SHIP MORTGAGE ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON MERCHANT MARINE

OF THE

COMMITTEE ON
MERCHANT MARINE AND FISHERIES
HOUSE OF REPRESENTATIVES

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

H.R. 3105

TO REVISE, CONSOLIDATE, AND ENACT LAWS RELATED TO MARITIME COMMERCIAL INSTRUMENTS AND LIENS AND PUBLIC VESSELS AND GOODS AS CHAPTERS 313 AND 315 OF TITLE 46, UNITED STATES CODE, "SHIPPING"

JUNE 28, 1988

Serial No. 100-78

Printed for the use of the
Committee on Merchant Marine and Fisheries

U.S. GOVERNMENT PRINTING OFFICE
90-206 WASHINGTON : 1988

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

H561-21

90-206 0 - 88 - 1

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SHIP MORTGAGE ACT

TUESDAY, JUNE 28, 1988

House of Representatives,
Subcommittee on Merchant Marine,
Committee on Merchant Marine and Fisheries,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:03 a.m., in room 1334, Longworth House Office Building, Hon. Walter B. Jones (Chairman of the Subcommittee) presiding.

Present: Representatives Jones, Hubbard, Lent, Miller, Bentley, Coble, and Davis.

Subcommittee staff present: Cynthia M. Wilkinson, Chief Counsel; Rudolph V. Cassani, Counsel; Gregory L. Lambert, Counsel; Ann M. Mueller, Clerk; Marlene Merchant-Bell, Staff Assistant; Kip Robinson, Minority Counsel.

Committee staff present: Ed Welch, Chief Counsel; Gerry Seifert, General Counsel for Maritime Affairs; John Cullather, Staff Assistant; Kurt Oxley, Assistant to Chief Counsel; George Pence, Minority Staff Director; Duncan Smith, Chief Minority Counsel; Rusty Johnston, Minority Counsel; Gwen Lockhart, Chief Minority Clerk; and Rebecca Feemster, Minority Counsel.

STATEMENT OF HON. WALTER B. JONES, A U.S. REPRESENTATIVE FROM NORTH CAROLINA, AND CHAIRMAN, SUBCOMMITTEE ON MERCHANT MARINE

Mr. Jones. The Subcommittee will come to order.

The Subcommittee hearing today is on chapter 313 of H.R. 3105, an Act to revise, consolidate, and enact certain laws related to maritime commercial instruments and liens as chapter 313 of title 46 of the United States Code.

In 1984, this Committee began codifying all of the maritime laws contained in title 46 of the United States Code. This process began with the vessel inspection and seaman protection laws in the 98th Congress. In the 99th Congress, the vessel load line and tonnage measurement laws were revised and codified into title 46. H.R. 3105 continues this process by codifying the Ship Mortgage Act, 1920. It also codifies the Suits in Admiralty and Public Vessel Act, but these will not be considered at this time. While the bill as introduced proposes to make no substantive changes to law, a number of witnesses will propose substantive changes that they believe will make vessel financing and mortgage recordation processes easier and more in keeping with modern practices.

While the Committee is willing to examine any and all suggestions for substantive change, we would like to move this legislation this year. Therefore, we will probably only adopt substantive changes that are of a noncontroversial nature and will not jeopardize the enactment of this legislation.

This is a law that Congress rarely examines. I look forward to hearing from the witnesses a review of the effectiveness of this law and to receiving their suggestions for improvements. I do believe that a number of modifications can be made that everyone, industry, Congress, and the Administration can agree to in an expeditious manner.

Our first witnesses are the Honorable John Gaughan, Administrator of the Maritime Administration and Captain Peter Lauridsen of the Coast Guard.

I ask at this point in the hearing that several statements be included, including one by Congressman Biaggi, Congressman Lent, Congressman Davis, and Congresswoman Bentley.

Without objection, so ordered.

[The prepared statements of Mr. Biaggi, Mr. Lent, Mr. Davis, and Mrs. Bentley follow:]

STATEMENT BY HON. MARIO BIAGGI, A U.S. REPRESENTATIVE FROM NEW YORK, AND VICE CHAIRMAN, COMMITTEE ON MERCHANT MARINE AND FISHERIES

Today's hearing is the continuation of this Subcommittee's efforts to codify existing maritime laws contained in title 46 of the United States Code. Chapter 313 of H.R. 3105 revises, consolidates, and enacts certain general and permanent laws of the United States related to commercial instruments and liens found in the Ship Mortgage Act, 1920. Chapter 315 concerns public vessels and goods presently contained in the Suits in Admiralty Act; however, this part of the proposed codification will not be considered at this time.

The Committee's first effort to codify the various laws under our jurisdiction began in 1983. We revised certain laws related to vessels and seamen as subtitle II of title 46, United States Code. This significant undertaking resulted in the repeal, reorganization, or revision of a number of antiquated statutes.

There is no doubt that the existing maritime laws of the United States have long been in need of major revision and codification. The Ship Mortgage Act, 1920 is no exception. I believe that the codification can be readily accomplished. What usually prevents us from moving forward expeditiously is the penchant to begin a noncontroversial revision and segueing into more substantive changes—either intentionally or unintentionally. Hopefully, the revisions will be either nonsubstantive or noncontroversial. The controversial changes must wait for consideration at a later date—when sufficient time can be devoted to studied review.

I also believe that we must consider any substantial revisions in ship mortgages in light of the extensive work that is presently taking place within the international maritime community. We must remember that any international changes could have an impact on our domestic law relating to maritime liens and mortgages.

In closing, I would like to thank the staff of the Office of Law Revision Counsel for their valuable assistance with the massive codification effort of title 46.

STATEMENT OF HON. NORMAN F. LENT, A U.S. REPRESENTATIVE FROM NEW YORK, AND RANKING MINORITY MEMBER, SUBCOMMITTEE ON MERCHANT MARINE

Mr. Chairman, I look forward to hearing the witnesses today to learn more about the Ship Mortgage Act and the technical and legal problems related to this law.

As our Committee works its way through the process of codifying the maritime laws, we have a unique opportunity to review some of these provisions, many of which have been in place for years. In some cases, it undoubtedly will be appropriate to make substantive changes to these laws to reflect our current economic and legal transactions as well as modern technology.

I will also be particularly interested to hear what the MARAD Administrator has to say about changes to the Bankruptcy Code. I thought we had solved the problems in the 1986 Bankruptcy Code revisions. Apparently there may be some additional problems that need addressing. I am pleased to note that the Administrator indicates in his remarks this morning that they are going to move forward in the next couple of months with the preparation of the report called for in the bankruptcy amendments. It is important for both the Transportation Department and the Commerce Department to submit those reports as soon as possible in order to give the Congress time to address these issues.

Thank you, Mr. Chairman.

STATEMENT OF HON. ROBERT W. DAVIS, A U.S. REPRESENTATIVE FROM MICHIGAN, AND RANKING MINORITY MEMBER, COMMITTEE ON MERCHANT MARINE AND FISHERIES

Mr. Chairman, I want to thank you for holding this hearing on H.R. 3105, a bill that will codify the provisions of the Ship Mortgage Act, 1920. This process of codifying all of the maritime laws contained in title 46 of the United States Code began a number of years ago with the codification of the vessel inspection and seamen protection laws, and continued in the last Congress with the codification and revision of the vessel load line and tonnage measurement laws.

I would be the first to admit that this is perhaps one of the least glamorous subjects that has come before us, but it is a necessary and vital service for those who use these laws on a daily basis. As public servants, we have a duty to make our laws clear, concise, and understandable. I commend you for continuing the effort begun in earlier sessions.

Mr. Chairman, last year I introduced H.R 3298, a bill that would attempt to centralize recordation of mortgages on recreational vessels. I bring this up now because I would hope the Subcommttee will give serious consideration toward incorporating certain provisions of H.R. 3298 relating to the Ship Mortgage Act into H.R. 3105.

Recreational boating is a growth industry in this country. As the popularity of boating increases, the number and complexity of financing transactions grows. We must provide adequate protection for the security interests of lenders in this area to encourage and support the boating industry and to assure that boaters can obtain bank financing for their boats. In addition, we must provide greater evidence of ownership for recreational vessel owners operating in States without boat titling laws. I believe that we can accomplish these changes and respond to the needs of recreational vessel owners and lenders in the context of H.R 3105.

Mr. Chairman, I look forward to working with you on this bill and hope we can see it enacted into law by the end of this Congress.

STATEMENT OF HON. HELEN DELICH BENTLEY, A U.S. REPRESENTATIVE FROM MARYLAND

Thank you, Mr. Chairman, and thank you, Mr. Lent, for calling this hearing on a bill that is overdue in offering financing relief to the millions of small boat owners throughout the United States, many of whom enjoy the pleasures offered by the Chesapeake Bay.

The current Ship Mortgage Act is archaic and, as result, has limited financing options to boat purchasers.

It has spawned a new industry that provides to boat purchasers the service of filing with the Coast Guard all of the complex documents required to certify these crafts. This filing process has added $200 to $300 to the cost of buying a pleasure craft.

This legislation provides an opportunity to simplify the Ship Mortgage Act in two important ways: one, it will assist boat owners in securing financing; and, two, it will enable banks and lending institutions to put financing in place at a low cost.

Mr. Chairman, I look forward to hearing the testimony of the various panelists today, and I want to pledge to you my support in moving this legislation through the Congress, because I believe it is absolutely essential to update current marine financing practices.

Thank you, Mr. Chairman.

Mr. JONES. The Chair recognizes the witness, Mr. Gaughan.

STATEMENT OF HON. JOHN GAUGHAN, ADMINISTRATOR, MARITIME ADMINISTRATION, DEPARTMENT OF TRANSPORTATION; ACCOMPANIED BY KARL E. BAKKE, CHIEF COUNSEL, AND RICHARD E. BOWMAN, ASSOCIATE ADMINISTRATOR FOR MARITIME AIDS

Mr. GAUGHAN. Thank you very much, Mr. Chairman.

Mr. Chairman, and Members of the Subcommittee, I am John Gaughan, the Maritime Administrator. I am accompanied today by Karl Bakke, the Chief Counsel of MARAD, and Mr. Richard Bowman of my agency.

It is indeed a pleasure for me to appear this morning to present the views of the Department on certain portions of H.R. 3105.

Specifically, I have been requested to testify on chapter 313 of H.R. 3105. That chapter, entitled "Commercial Instruments and Maritime Liens," is generally intended to recodify the Ship Mortgage Act, 1920, presently set forth in section 30 of the Merchant Marine Act, 1920. The Maritime Administration's interest in proposed chapter 313 arises from our responsibilities under the Merchant Marine Act, 1936, and the Shipping Act, 1916.

Mr. Chairman, the Merchant Marine and Fisheries Committee is to be commended for efforts to codify the various provisions of law now set forth in the Appendix to title 46, United States Code. This codification is a formidable undertaking, of which H.R. 3105 is but one element. Therefore, I am pleased to inform you that the Maritime Administration generally supports H.R. 3105 as a bona fide effort to consolidate topically related provisions of law in an organized fashion, particularly as it clarifies and conforms provisions to accommodate current requirements for commercial instruments and maritime liens.

On December 8, 1986, the Department commented extensively on H.R. 3158, which is identical to H.R. 3105. My comments are generally consistent with the Department's stated views.*

As the Members of this Subcommittee are aware, commercial law in general, and maritime law in particular, need certainty and clarity to work effectively. Individuals extending credit to vessels and engaging in maritime transactions need to be certain of their rights and obligations. Without such assurances, they will hesitate to extend credit and the flow of commerce will slow.

H.R. 3105 goes beyond the codification of existing law and contains provisions that make substantive changes, as you noted. We recognize that the Ship Mortgage Act has been in effect almost 70 years and, since its enactment, maritime transportation and commercial law have undergone major changes. Therefore, the Maritime Administration also generally favors the substantive changes you have proposed in this portion of the bill. I would simply like to express a caveat concerning the vehicle of codification as appropriate for this purpose. We believe that substantive changes in law should be the subject of separate legislation.

Despite our general support of H.R. 3105, we would suggest some changes which I believe would help perfect this proposed legislation. The Department would be pleased to meet with you or members of your staff to discuss these changes. I will highlight a few of those that we would suggest.

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* [EDITOR'S NOTE.—Referenced letter can be found at end of hearing.]

There is a concern in the maritime industry that use of the word "indebtedness" in the Ship Mortgage Act was intended only to apply to loans with a fixed amount, and thus fails to apply to revolving lines of credit, guarantees, or contingent liabilities. Section 31322 of H.R. 3105 should be clarified to make it clear that a preferred mortgage can secure these additional types of conventional commercial arrangements.

Under current law, a U.S. District Court can appoint a receiver to operate any seized vessel. Through this device the costs of caring for a vessel during foreclosure proceedings can be reduced. However, this procedure is rarely used because the question exists as to whether the District Court loses legal authority over a vessel once it leaves the geographic confines of the jurisdiction, and few maritime commercial operations occur within one judicial district. Section 31325(e) of H.R. 3105 should be clarified to provide assurance that a District Court continues to retain jurisdiction over a vessel in receivership, whatever its subsequent location.

We propose deletion of section 31322 (a)(6) from H.R. 3105, which restates the current law and causes a mortgagee to lose its preferred mortgage if it waives its preferred status. The provision is not clear as to what exactly is a "waiver of preferred status," nor what purpose is served. This language unnecessarily complicates the process of restructuring indebtedness or subordinating liens, and compromises the flexibility of the Maritime Administration in negotiating workout terms to protect the Government's financial interests in the vessel assets of distressed obligors.

Present law does not expressly include the United States of America among the parties eligible to hold a preferred mortgage. If the recodification is to include new substantive law, it should make clear that the Government is an entity entitled to be a mortgagee on a preferred basis.

Two provisions about which the Department has reservations deserve special comment.

First, current law prohibits any entity not a citizen of the United States (within the terms of 46 App. U.S.C. 802) from purchasing a vessel at a foreclosure sale. H.R. 3105 would allow a non-U.S. citizen to effect such a purchase with the consent of the Secretary. The Maritime Administration has taken the position that current law also prohibits a trustee-mortgagee for a foreign beneficiary from purchasing the mortgaged vessel on behalf of that foreign beneficiary at a foreclosure sale. The Department is opposed to a general change in current law, but has considered at length the problems of a purchase by a trustee-mortgagee for foreign-citizen beneficiaries. We are in sympathy with the problems faced by the trustee-mortgagee for foreign-citizen beneficiaries participating in a foreclosure sale to protect its interest. We believe, however, that the language should carefully circumscribe the extent of this participation. In particular, the trustee-mortgagee for foreign-citizen beneficiaries should be allowed to purchase the vessel only for resale. Any subsequent resale would be subject to the usual limitations on vessel sales. My staff would be pleased to work with your staff on acceptable alternatives addressing concerns of the drafters.

Second, H.R. 3105 would perpetuate the current requirement in the Ship Mortgage Act that, to be valid, a preferred ship mortgage must be endorsed on the vessel's certificate of documentation. While such endorsement may once have had utility, in a world of modern communications, this requirement has largely become an unnecessary burden on commerce. Compliance with this endorsement provision has also been a burden on the Maritime Administration, delaying the perfection of our mortgages, complicating closings, and increasing the effort required to ensure that transactions are properly completed.

Mr. Chairman, this concludes my remarks on H.R. 3105. However, I would like to speak briefly to another matter, our proposed modifications to the Bankruptcy Code.

The Administration has recently proposed to make permanent the Maritime Administration's temporary exemption from the statutory stay of creditors' rights for an indefinite period following filing of a bankruptcy petition, now found in 11 U.S.C. 362(b)(12). This authority, Mr. Chairman, was provided to us as a result of the cooperative effort of the Congress, your staff, and the maritime industry which was being affected by competitors who had been relieved of the obligation to pay title XI capital costs as a result of the bankruptcy filings.

I cannot overemphasize the importance we place on the need to continue the right of the Maritime Administration to foreclose on a title XI mortgage or other vessel security interest 90 days after the filing of a bankruptcy petition. This is important for two primary reasons: one, the protection of the Government's financial interests; two, the overall health of the viable portions of the United States maritime industry.

It is important that Congress begin deliberation of the Administration's proposal as soon as possible. Our current authority expires at the end of 1989.

Staff of the Committee have asked me when the Maritime Administration will complete the Congressionally-required report on the effects of section 362(b)(12). A report on the effects, together with any recommendations for further legislation, is due not later than July 1, 1989. However, in light of my view of the importance of this legislation and the staff's interest, I have accelerated the drafting of this report. I expect to provide you with a copy within the next few months.

Allow me to tell you quickly that the Maritime Administration has found the exemption from the automatic stay very beneficial. This conclusion is supported not only by our experience in the bankruptcy cases that have been filed after passage of section 362(b)(12), but also in other cases of financial distress and defaults that have led to reasonable financial solutions for the taxpayer because the alternative of lengthy delays in bankruptcy court for the debtor was no longer a viable option, and thus bankruptcy filings were avoided.

Prior to the 1986 bankruptcy legislation, which allowed us to lift the automatic stay after 90 days, some debtors used bankruptcy filing as a threat in negotiations. In effect, they were in a position to say, accept my workout proposal, or I will declare bankruptcy and continue to control my equipment for years without significant capital costs. Limiting the stay to 90 days has eliminated that option and opened the door for a more balanced discussion of the Government and taxpayers' interest against the debtors.

Mr. Chairman, under the statutory provision, the Maritime Administration has been able to more expeditiously repossess vessels from financially moribund debtors. This has had the benefit of protecting other operators who can find themselves in a prolonged precarious situation resulting from being forced to compete with an operator that through bankruptcy has been relieved of the obligation to pay its capital costs.

The Government has also benefitted by being able to liquidate its collateral more promptly. At the same time, the agency has been able to exercise the discretion to refrain from foreclosing on debtors who have demonstrated a strong likelihood of developing a feasible reorganization plan.

The bankruptcy involving U.S. Lines, even though the company did not ultimately survive, is a good example of this. In that case, in an effort to help the company work on a reasonable reorganization, we carried out lengthy discussions with the carrier and the various creditor committees. When it became clear to all that a plan was not possible, an agreeable liquidation plan was put together, one which maximized the Government's return while minimizing unnecessary and costly adversarial litigation.

We have not, however, been able to take as full advantage of the law as we believe Congress intended. In a number of cases, bankruptcy courts have enjoined the United States from pursuing its rights even after the initial 90-day grace period. The current legislative proposal would address that issue by restricting the injunctive powers of the bankruptcy courts, thereby ensuring that the balance drawn by Congress is not redrawn.

Mr. Chairman, I recognize that in the absence of our report you and your staff do not have the advantage of the quantitative data you need to make an informed judgement of this issue. Because of that, I have accelerated preparation of the report and will have it to you within a few months. My staff and I look forward to working with you to keep this important legislation in place.

Mr. Chairman, this concludes my prepared remarks. After Captain Lauridsen, I will be glad to answer any questions that you or the Members of the Subcommittee may have.

Mr. JONES. Thank you, Mr. Gaughan.

Do any other members of your panel want to testify?

Mr. GAUGHAN. No, sir.

Captain Lauridsen does have a statement.

Mr. JONES. Captain Lauridsen, you are recognized, sir.

STATEMENT OF CAPT. PETER C. LAURIDSEN, USCG, DEPUTY CHIEF, OFFICE OF MARINE SAFETY, SECURITY, AND ENVIRONMENTAL PROTECTION, HEADQUARTERS, U.S. COAST GUARD, ACCOMPANIED BY THOMAS L. WILLIS, CHIEF, VESSEL DOCUMENTATION BRANCH

Captain LAURIDSEN. Good morning, Mr. Chairman.

I am Captain Peter Lauridsen, Deputy Chief of the Office of Marine Safety, Security, and Environmental Protection.

I appreciate this opportunity to address you and the other distinguished Members of this Subcommittee on H.R. 3105, a bill which, in part, would codify the Ship Mortgage Act. I am accompanied this morning by Mr. Thomas Willis, Chief of the Vessel Documentation Branch of the U.S. Coast Guard.

The Coast Guard's major interest in H.R. 3105 is in proposed chapter 313 of the United States Code, entitled "Commercial Instruments and Maritime Liens." That chapter is generally intended to codify the Ship Mortgage Act, 1920. The Coast Guard is the agency charged with recording instruments under the Act. In addition, the Coast Guard has responsibilities pursuant to the Shipping Act, 1916 and the Merchant Marine Act, 1936, which would be affected by this bill.

The Merchant Marine and Fisheries Committee has performed exemplary service in the codification effort. The Coast Guard is pleased to confirm its support for most of the provisions of H.R. 3105.

H.R. 3105 is more than an effort at codification of existing law in that it contains provisions that make substantive changes. Many of the changes are welcome in that they reflect modern practice and recognize modern business requirements. Those changes will result in a difference in the way the Coast Guard carries out its responsibilities under the law and provide for more efficient service to the public.

From the Coast Guard's perspective, the greatest single change occasioned by H.R. 3105 would be its facilitation of recordation of purchase money mortgages. Such mortgages, which were not contemplated in the Ship Mortgage Act, 1920, constitute the vast majority of instruments submitted for recordation.

One of the requisites for preferred status under the present statute is that the mortgage at the time that it is made must cover the whole of a vessel of the United States. In view of that requirement, vessel mortgages cannot be made until after the vessel has been documented. In most cases, this means that mortgages cannot be submitted for recordation until after a certificate of documentation has been issued. The provisions of the codification would allow mortgages to be submitted with other instruments, such as bills of sale, which relate to the same transaction.

Despite our overall support for the measure, there are a few technical areas in which the Coast Guard feels that the bill could be improved. In this connection, the Department provided detailed comments on the bill as introduced during the last Congress. We would be happy to submit those comments again.

[Editor's note.—DOT letter of 8 December 1986 can be found at end of hearing.]

Captain **Lauridsen**. In addition, the Coast Guard would like to identify reservations we have with certain provisions of H.R. 3105.

At proposed section 31322(a)(4), and elsewhere, H.R. 3105 continues the requirement found in present law which requires that a ship mortgage be endorsed upon the vessel's certificate of documentation in order to attain preferred status. Endorsements are generally burdensome, both to commerce and the Government. Situations frequently arise under current practice where a vessel must sail in foreign waters without its primary evidence of nationality because the certificate of documentation has been submitted to the Coast Guard for endorsement.

During the past calendar year, more than 100,000 mortgages and related instruments were recorded and endorsed by the Coast Guard. Elimination of the requirement for endorsements would assist in relieving backlogs at our busier ports of documentation. In addition, computerization of vessel encumbrance histories, a projected Coast Guard modernization effort, would be easier without the need for endorsements.

At proposed section 31321(b)(4), H.R. 3105 requires that instruments be acknowledged before a notary public or other public official authorized by a law of the United States or of a State in order to be recordable. It is suggested that this requirement be modified in two ways:

First: In addition to an acknowledgment, a jurat or similar notarization should be authorized to satisfy this requirement.

Second: Many transactions take place outside of the United States. Generally, the only persons outside of the United States authorized to take acknowledgments are consular officers and military officers. It is often difficult to appear before one of those persons. Inasmuch as the United States is a party to the Hague Convention abolishing the requirement of legalization for foreign public documents, it is suggested that foreign notarizations, legalized by a certificate pursuant to the convention, be granted the same status as notarization in the U.S. for instrument recordation purposes.

For these reasons we believe that acknowledgements, jurats, and notarizations performed in accordance with the laws of the various States and notarizations conforming to the Hague Convention issued in countries which are parties to the convention should be authorized for purposes of this section.

At proposed section 31322(a)(4), H.R. 3105 continues the requirement for an affidavit of good faith by the grantors of a preferred mortgage. Such affidavits are of little, if any value, and usually serve only as a hindrance to the transaction. Moreover, recent court decisions have added to uncertainty as to who may make an affidavit of good faith. The Coast Guard recommends that this requirement be dropped.

H.R. 3105 does not carry forward the requirement found in subsection C of the Ship Mortgage Act, 1920 that recordation of instruments be accomplished at the home port of the vessel. Under the current system, accurate indexing is possible only if recordation is restricted to the home port. The Coast Guard, therefore, recommends inclusion of such language.

Our last major area of concern, Mr. Chairman, is the provision in proposed section 31304 for Government liability in the event that a person who makes a contract secured by or on the credit of a documented vessel which is covered by a mortgage suffers a loss because the Secretary failed to comply with a provision of the chapter. Such a provision constitutes an unusual and undesirable waiver of sovereign immunity. Consequently, we recommend that this provision be deleted.

Although the Coast Guard has reservations about possible interpretations of certain language within the bill, any uncertainties can be resolved through cooperation of our respective staffs. The Coast Guard will be happy to cooperate in such an effort, including, if appropriate, drafting assistance.

Mr. Chairman, this concludes my prepared remarks on H.R. 3105. I shall be happy to answer questions which you or Members of the Subcommittee may wish to pose. I assure you that any questions submitted to us later in writing will be answered in a timely fashion.

Thank you, Mr. Chairman.

Mr. JONES. Thank you, Captain Lauridsen. Mr. Barnett of the Maritime Law Association of the U.S. and Mr. King of the American Bar Association have made a number of recommendations for substantive changes. Please give us your view of each of these recommendations briefly, sir, if you're familiar with them.

Captain LAURIDSEN. Mr. Chairman, I'm not familiar with substantive changes.

Mr. JONES. Would you please submit your answer to the record once you research it?

Captain LAURIDSEN. We would be happy to, Mr. Chairman.

Mr. JONES. All right, sir.

[The information follows:]

COMMENTS ON SUGGESTIONS

The Coast Guard concurs with most of the suggestions put forth by Mr. King and Mr. Barnett. The proposals with which the Coast Guard concurs include:

a. elimination of the requirement for the Affidavit of Good Faith.

b. elimination of the requirement that a mortgage not stipulate that the mortgagee waives preferred status.

c. clarification of the provisions dealing with the amount of mortgage to facilitate indexing multi-currency loans or revolving credit loans, which have become commonplace in ship financing.

Mr. Barnett also suggests eliminating the requirement that mortgages be endorsed upon Certificates of Documentation in order to attain preferred status. The Coast Guard agrees.

Mr. Barnett proposes that mortgages become effective on filing; i.e., when presented to the Coast Guard for recordation. Mr. King proposes that "notices of mortgage be recorded" in lieu of entire mortgage instruments. This latter suggestion follows the Uniform Commercial Code. The Coast Guard believes that Mr. Barnett's proposal would be difficult to implement. While there is no objection to Mr. King's proposal per se, failure to record the entire instrument may weaken the constructive notice given to prospective lienors.

The Coast Guard concurs with Mr. Barnett's suggestion calling for clarification of the jurisdiction of certain territorial courts.

Mr. Barnett's third suggestion concerning the ability of Westhampton trustees to bid at foreclosures sales, deals with a policy matter not within the purview of the Coast Guard. This is a question which would more properly be answered by the Maritime Administration.

Other suggestions made by Mr. King regarding foreclosure, subordination agreements, and finance leases are policy matters which have little impact upon the Coast Guard, and are not properly subjects for Coast Guard comments.

Mr. JONES. What is your opinion on the recommendation by Mr. King that the Ship Mortgage Act more closely follows the Uniform Commercial Code?

Captain LAURIDSEN. Mr. Chairman, we're studying the proposal. We generally favor it, although, because the study is not complete, we would hesitate to offer a positive statement at this time.

Mr. JONES. Would you furnish that for the record, once your research is completed.

Captain **Lauridsen**. Yes, sir. We would be more than happy to, sir.

Mr. **Jones**. All right, sir.

[The information follows:]

Uniform Commercial Code Suggestion

While there are certain advantages in having the Ship Mortgage Act closely follow the Uniform Commercial Code, it must be remembered that the Uniform Commercial Code is drafted to deal almost exclusively with domestic financing. The Ship Mortgage Act, on the other hand, must be capable of enforcement in foreign as well as domestic courts. The Coast Guard would not oppose Mr. King's recommendation insofar as its implementation would not weaken international recognition and enforcement of ship mortgages.

Mr. **Jones**. Is it necessary to retain a provision that requires notification of the Coast Guard and endorsements on documents when the mortgage is fully discharged?

Captain **Lauridsen**. Yes, sir.

Mr. **Jones**. Why?

Captain **Lauridsen**. Mr. Chairman, I'd like to ask Mr. Tom Willis to answer the remainder of the question.

Mr. **Jones**. All right, sir.

Mr. **Willis**. Our concern, Mr. Chairman, with receiving a notice of discharge is that we cannot allow the document to be surrendered while a mortgage remains outstanding of record. At the present time, we have numerous vessels whose documents are current only for purposes of the Ship Mortgage Act. We would like to eliminate this recordkeeping problem and also some misleading statistics as to the state of the U.S. merchant marine.

An additional consideration is the fact that, in the absence of a recordable satisfaction, a purchaser of the vessel may not be able to obtain documentation and may be unable to use the vessel for commercial purposes.

Mr. **Jones**. Captain Lauridsen, under current law you can only record a mortgage for a documented vessel. The bank won't give you the money to own the vessel unless there is a perfected mortgage. You can't perfect a mortgage because you can't document it since you don't own it. Can this "Catch 22" be fixed by eliminating the vessel documentation requirement and substituting other criteria, or by having the mortgage deed recorded on the date of receipt of the acceptance as done by the FAA rather than the date on which it is actually recorded?

Captain **Lauridsen**. Mr. Chairman, again, I'd like to ask Mr. Tom Willis to respond to that one.

Mr. **Jones**. Mr. Willis.

Mr. **Willis**. We believe, Mr. Chairman, that the current language in the bill eliminating the requirement that the vessel be a vessel of the United States at the time the mortgage is made goes a long way toward permitting this.

We concur with the intent that the mortgage attain preferred status upon recordation. This is one of the reasons we would like to do away with the endorsement. We are concerned with being more responsive and facilitating vessel financing. We believe that the changes already here, with some slight adjustment, will take care of that problem.

Mr. JONES. All right, sir. Thank you very much.

Mr. Gaughan, your statement seems to indicate that MARAD has the responsibility to protect the competition. Some allege that in the WFI [Woeck Family Industries] reorganization you ignore this role and function solely as a creditor would. How can you reassure us that the cynics among us are wrong?

Mr. GAUGHAN. Mr. Chairman, if I could first of all just give some quick background on WFI.

WFI is an operator in the Pacific Northwest that filed for protection in 1986. Since February of 1986, there have been a number of efforts at reorganization. The latest is an Employee Stock Ownership Plan [ESOP] which is presently before the bankruptcy court. That court held a hearing earlier this month where it approved the ESOP's disclosure statement and has now ordered a vote on the plan of reorganization.

As we have worked with the ESOP and the other creditors, one of our foremost concerns has been the competitive impact. I believe that a report that was done by the competitors confirms MARAD's long-held view that the reintroduction of equipment by WFI will not upset the competitive balance in that trade.

There continue to be concerns expressed by competitors that the projections associated with WFI's reorganization plan may be too optimistic. We, as a creditor, are privy to proprietary information that isn't available to them, and we are continuing to make our review to ensure that those projections are reasonable. We are in that process with an eye towards making a recommendation on the reorganization plan, sir.

I would add simply to that, Mr. Chairman, that throughout all of these bankruptcies I have had two primary concerns. One is the balancing of the fiduciary responsibility I have to recover funds for the American taxpayer. But, second is a keen sense of MARAD's responsibility as the promoter in this industry and to ensure that we do not upset unreasonably the competitive balances in the various sectors. I think we have shown that sensitivity throughout a whole range of financial transactions. I would hope that in the final analysis that's the view in WFI. That certainly is the same goal.

Mr. JONES. Thank you.

Mr. GAUGHAN. Yes, sir.

Mr. JONES. How can we convince the Judiciary Committee that you have a unique requirement when you just function like any ordinary creditor?

Mr. GAUGHAN. Mr. Chairman, I would respond to that this way. First of all, the nature of the equipment involved here is entirely different. This equipment can move in and out of jurisdictions and, in fact, operate even outside of the United States.

Because of MARAD's particular role in the promotion and the financing of the industry, we are not talking about one house that may be in a market of thousands. There are situations where you can have a large number of vessels that can, in fact, have a significant impact on the particular segment.

We have had experiences prior to the enactment of the bankruptcy statute where cases went on for three years. The vessels operated in the marketplace without having to pay back their capital to the detriment of the rest of the market, some of which also had Government-guaranteed financing behind them.

Certainly, since enactment of the provision, those timeframes in many cases have come down significantly. We have been able to get control of the equipment and balance the, in some cases, very tender nature of the economics in the sector to ensure that it was not further disrupted, sir.

Mr. JONES. Thank you.

Mr. GAUGHAN. I might add if I could, sir, that this is not serving as a prototype, if you will, to open the floodgates for the rest of the Government. There is no plan to extend it to other programs. I certainly have not been engaged in any discussions elsewhere in the Executive Branch to use this as the nose under the tent to reintroduce the Federal Government.

Mr. JONES. But it has been said that the Government has nothing to lose and that if a plan fails you can recover the assets. Is there an element of truth in this?

Mr. GAUGHAN. Well, there certainly is truth in the fact, sir, that if a plan of reorganization does not make it that we have not given up our rights to that equipment. But we certainly recognize—as I said before, as we look at reorganizations—that we have a responsibility to ensure that the capital costs that we are placing on the equipment that would be part of a reorganization plan reflect the fair market value of that equipment, so as not to put that company in an unfair competitive position.

It is often the case that we have rejected out-of-hand initial reorganization plans primarily because the debtors have attempted to put together a plan that didn't have fair market values associated with the equipment. We just simply will not participate in a reorganization that way. We have to be convinced that there is a reasonable opportunity—certainly not a certainty that the reorganization plan will succeed—but a reasonable certainty, along with requisite fair market value cost to the equipment.

Mr. JONES. Thank you.

Finally, Mr. Gaughan, would you submit for the record where in the WFI plan is the right to recover the asset, and the assurances that are being sought by the competition that there are safeguards built into the proposal?

Mr. GAUGHAN. Yes, sir. Subject to counsel telling me that it's proper to do that, we will provide all of that. I don't say that to duck the question.

Mr. JONES. Right. Thank you.

[The information follows:]

ASSET RECOVERY AND SAFEGUARDS

Article III to the Debtors' Third Revised Joint Plan of Reorganization, "Treatment of Classes," provides not only safeguards for early warning if the debtor is unable to meet its obligations to MARAD, but also recovery rights in the event of default.

Class 6, Allowed Secured Claims of the U.S. Department of Transportation Acting Through the Maritime Administrator (MARAD).

B. *Secured Notes* provides: "Payments of principal and interest are unconditionally due quarterly on a calendar quarter basis in arrears after the Effective Date, * * * as required by the terms of the series A Notes."

D. *Other Provisions* provides: "In the event of default the Debtor unconditionally agrees to deliver to MARAD the vessels upon MARAD's demand."

Mr. JONES. Mr. Coble.

Mr. COBLE. Thank you, Mr. Chairman.

Mr. Chairman, we have prepared some questions, most of which are technical and most of which are time consuming. Without objection, I would like to submit those questions and then have the answers forthcoming.

Mr. JONES. In view of the time element, it is so ordered.

Mr. COBLE. Thank you, sir.

Mr. JONES. All right.

Mr. JONES. Mr. Miller.

Mr. MILLER. I make a proposal for questions and answers. I will follow the same path as Mr. Coble.

Mr. JONES. The Gentleman makes the same request as Mr. Coble. Is that correct?

Mr. MILLER. Right.

Mr. JONES. Without objection, so ordered. The Gentleman may submit his technical questions.

Mrs. Bentley.

Mrs. BENTLEY. Well, I think I better follow the pattern set by my two colleagues here or they might step on my toes. But I do have a statement I would like to have included in the opening. I would ask unanimous consent——

Mr. JONES. The Gentlelady's statement will be inserted in the record without any objections.

[The prepared statement of Mrs. Bentley can be found of the beginning of the hearing.]

Mr. JONES. Also, you will submit your questions to the record?

Mrs. BENTLEY. Yes.

Mr. JONES. That concludes the appearance of Panel No. 1. I thank each of you gentlemen for your presence here this morning.

Mr. GAUGHAN. Thank you very much for your courtesy, Mr. Chairman.

Mr. JONES. Mr. Gaughan, did we get you out in time?

Mr. GAUGHAN. Sir?

Mr. JONES. Does this get you out in time?

Mr. GAUGHAN. Yes, sir.

Thank you very much, Mr. Chairman.

Mr. JONES. Thank you.

The Chair now recognizes Panel No. 2 consisting of Mr. Richard B. Barnett, Mr. C. Peter Theut, Mr. Bruce King, and Mr. John C. Moriniere.

The Chair recognizes the gentlemen. Who proposes to lead off? Mr. Barnett.

STATEMENT OF RICHARD B. BARNETT, CHAIRMAN, COMMITTEE ON MARINE FINANCE, THE MARITIME LAW ASSOCIATION OF THE UNITED STATES; C/O HEIGHT, GARDNER, POOR & HAVENS, NEW YORK, NY

Mr. BARNETT. Mr. Chairman, and Members of the Committee, I thank you for the opportunity to appear before you this morning. I am here as Chairman of the Marine Finance Committee of the Maritime Law Association.

I have with me in the audience the former chairman of the Marine Finance Committee, Emory Harper. Also Robert Fisher, who is Chairman of our Yacht Subcommittee, and David Williams, who is Secretary of the Marine Finance Committee.

I would like to summarize the contents of my statement, if I may. The statement was submitted last Friday.

Mr. JONES. Without objection, your prepared statement will appear in the record immediately following the oral presentations. The gentleman is recognized for brief comments.

Mr. BARNETT. The Maritime Law Association has more than 3,200 members who are engaged in the practice of maritime law. Our Marine Finance Committee has 80 members, all of whom work with the provisions of the Ship Mortgage Act on a day-to-day basis representing lenders and shipowners.

We obviously have a great interest in the Act and the proposal for the recodification. We look upon this as an opportunity to make some changes in the Act which we think would benefit the industry. We recognize that major changes in the Act are really not feasible at this time. We have tried to restrict our recommendations to a few that we think we can reach general agreement on with members of the Government, and also to certain other provisions which we believe are particularly important.

The Ship Mortgage Act has worked well over the years since 1920, but we do believe some minor modifications are in order to accomplish three primary purposes:

First, to enable the Ship Mortgage Act to accommodate modern financing techniques which have developed since 1920.

Secondly, to eliminate certain of the formal requirements in the Act that experience has shown are unnecessary or obsolete.

Third, to clarify certain provisions in the Act which court rulings and agency rulings have shown are in need of clarification.

Our recommendations which have been developed by the Marine Finance Committee have been endorsed, by the way, by the Maritime Law Association's Executive Committee and represent the position of the Association at this time.

Our first recommendation is that certain of the formal requirements which must be met for a valid mortgage to attain preferred mortgage status be eliminated. These requirements are:

First, that the mortgage particulars be endorsed on the ship's certificate of documentation; second, the requirement for an affidavit of good faith; and third, the requirement that the mortgage not stipulate that the mortgagee waives the preferred status.

All of these provisions add unnecessary complications and expense to a ship financing transaction and, in our view, no longer serve any useful purpose.

Second, we recommend that the provisions dealing with the amount of the mortgage be clarified. When the Ship Mortgage Act was adopted, the typical ship financing transaction was a very simple one in which a loan was made to be repaid with simple interest over a fixed number of installments.

Today, ships are financed by a variety of financing options including revolving credit loans, letters of credit, and multi-currency options. These financing arrangements do not always fit comfortably within the framework of the Ship Mortgage Act. We believe that by making some changes in the definition of amount of the mortgage that the modern financing techniques could be comfortably included within the framework of the Ship Mortgage Act.

Our third recommendation is one that has aroused a great deal of support and concern in the shipping industry. That involves the ability of a Westhampton trustee to purchase a U.S.-flag ship at a foreclosure sale in the United States. The Ship Mortgage Act requires that the mortgagee be a citizen of the United States and provides that upon foreclosure the vessel must be sold to a citizen of the United States within the meaning of section 2 of the Shipping Act.

Foreign lenders are encouraged to participate in the financing of United States-flag vessels by the mechanism of Public Law 89–346 which was adopted in 1954. Under these provisions, the foreign lenders designate a United States citizen corporate trustee to hold the mortgage for their benefit.

The Government agencies have taken the position that, while this Westhampton trustee, as it is called, can institute a foreclosure proceeding, the Westhampton trustee cannot bid on the vessel and buy it in at the foreclosure sale. This puts the foreign lenders at a marked disadvantage compared to United States lenders because if market conditions are bad, as they generally are when the foreclosure takes place, the only way a lender can hope to recover its investment is to buy the ship at the foreclosure sale and hold the vessel until the market conditions improve.

The United States shipping industry has been a troubled industry over the years. The shipowner faces a limited market for his financing needs. Right now, many foreign lenders are reluctant to participate in the financing of United States-flagged vessels unless there is a clarification of the right of the Westhampton trustee to bid in at the foreclosure sale. We urge that the law be clarified in this respect so that foreign lenders can be on a more equal footing with domestic lenders in the financing of ships.

I would point out again that the ships purchased by the Westhampton trustee at the foreclosure cannot be transferred to foreign registry and cannot be sold to a non-citizen without Maritime Administration approval.

Our fourth recommendation is that the jurisdiction of certain territorial courts should be clarified. In particular, there have been problems with the High Court of American Samoa. I think it's important that that court have jurisdiction to foreclose mortgages on vessels particularly because of the fishing industry vessels that trade there.

Our fifth and final recommendation is that mortgages and other instruments should be valid when filed for recording. This recommendation is particularly important to the yacht financing industry. Years ago, one could count on a mortgage being recording substantially simultaneously with its submission to the Coast Guard. Over the years now a backlog has developed in many cases. Sometimes months lapse between the time the mortgage is filed for recording and the time the actual recording takes place.

We have suggested that the Federal Aviation Act provisions which provide that an instrument shall be effective from filing be considered as a model for changes in the Ship Mortgage Act to make instruments effective when filed rather than when the recording takes place.

We urge the adoption of the foregoing recommendations. We believe that the effect will be to benefit the shipping industry by facilitating the financing of ships. We would be pleased to work with the staff on language to accomplish these purposes.

That concludes my statement. On behalf of the Maritime Law Association, I thank you for the opportunity to appear here.

[The prepared statement of Mr. Barnett can be found at end of hearing.]

Mr. JONES. Thank you.

Who is next? Mr. Theut.

STATEMENT OF C. PETER THEUT, GENERAL COUNSEL, NATIONAL MARINE BANKERS ASSOCIATION, C/O BUTZEL, LONG, GUST, KLEIN & VAN ZILE, DETROIT, MI

Mr. THEUT. Mr. Chairman, I am Peter Theut. I am General Counsel for the National Marine Bankers Association. I wish to take this opportunity to thank the Committee for allowing me to speak with you very briefly today.

I am General Counsel for NMBA. The National Marine Bankers Association consists of about 144 major marine lenders in the United States with recreational boat loan portfolios in excess of $4 billion.

We have previously submitted the statement of our Executive Director, Mr. Gregory Proteau. I think Mr. Proteau's statement emphasizes the two major concerns that the recreational marine lending industry has in connection with any changes in the Ship Mortgage Act. I would like to take this opportunity to emphasize the two points that Mr. Proteau has made in his statement by reading paragraph 2 as follows:

"The first concern of the Association is that lien perfection afforded by the Ship Mortgage Act of 1920 is an excellent way to secure loans made on a so-called documentable vessel. Though ponderous and perhaps archaic, gaining a first preferred ship's mortgage on large boat transactions is a routine practice by the majority of our members. We are amenable to changes proposed which would simplify and/or clarify the lien procedure; however, we would oppose any revisions that would in any way lessen the impact of the ship's mortgage or dilute its value as a security instrument. The National Marine Bankers Association continues to discuss this issue regularly with members of the maritime law community and defers to its expertise in determining which changes would be beneficial or detrimental to the marine community at large. We would also encourage the Committee to continue its dialogue with admiralty attorneys along those lines."

The second major concern of the Association is contained in Mr. Proteau's third paragraph.

"A second, much broader area also merits commentary. While the National Marine Bankers Association members—and the documentable boat-owning populace—enjoy the protection afforded by the first preferred ship's mortgage, America's small boat lenders and owners share no similar, uniform method of lien perfection.

Consider for a moment that in the United States for every registered pleasure boat above 26 feet, there are 40 registered boats below that length. Although you can place a ship's mortgage on those recreational vessels of 28- to 30-feet in length, how do lenders secure loans on smaller vessels?"

Those are the two major concerns of the National Marine Bankers Association.

[The prepared statement of Proteau can be found at end of hearing.]

Mr. THEUT. Our goals with respect to those concerns are, first of all, to continue to work closely with organizations like the Maritime Law Association and the American Bar Association's Admiralty Committee, as well as the Members of this Subcommittee, to hopefully strengthen and clarify the Ship Mortgage Act.

Our second goal is to work with the various States, as we have for a number of years now, to promulgate a uniform titling act that hopefully would apply to vessels that are not documentable.

We also would look forward to working with the States in an effort to promulgate a national lien recording system perhaps somewhat similar to that utilized by the FAA.

I would like to comment very briefly on three major problems that the recreational marine lending community has been confronted with in connection with the Ship Mortgage Act.

The first is the so-called infamous "gap" period. I am certain you are all very familiar with the "gap." It has been mentioned two or three times this morning already that the marine lending community often loans money and must wait for a considerable period of time before the mortgage instruments are perfected. That "gap" period has caused a considerable concern in the marine lending community. It has, in fact, caused some of the lenders to stay out of the market.

The second major problem is the problem confronting us with a dual filing system. The problems inherent in State filing systems as they relate to Federal filing systems are extremely complex. I am sure you have all studied those thoroughly. Nevertheless, they continue to be very perplexing to the marine lending community.

The third problem is an increasing number of State court interpretations and some lower Federal court interpretations of the Ship Mortgage Act. We find those interpretations somewhat puzzling to say the least. They have created major concern in the marine lending community. We are approaching those three problem areas in the following ways.

With respect to the "gap" situation, we are aware—as you are—that the U.S. Coast Guard has done a better job in recent years in closing that gap. We also very much appreciate efforts on the part of this Committee, as well as the MLA and the American Bar Association, to push for some sort of change that would make the mortgage effective upon filing. It probably would be the most desirable thing from the standpoint of the National Marine Bankers Association.

With respect to dual filing systems, this obviously is not an ideal world. I feel, however, that the only way that the problems inherent in the dual filing system can ultimately be approached is to have one system based on the Ship Mortgage Act for documentable vessels and then another uniform system that would apply to vessels that are not documentable. It would remain for this Committee, or perhaps some of the associations we are dealing with, to decide where that cutoff is. I don't think it necessarily has to be at the around 26-foot length that we presently have in the Act. It could be as high as 40 feet or 50 feet. I would not recommend anything lower than 30 feet.

With respect to some of the lower court interpretations recently, the National Marine Bankers Association has fostered the creation of a network of admiralty lawyers throughout the United States. There are seven such firms that we have asked to monitor—I was going to say fast breaking legislation, but that really doesn't often happen—legislation as well as fast-breaking case law in certain recreational boating areas of the country so that, hopefully, we can file amicus briefs a little earlier than we have in the past and see if we can clarify some of those decisions.

I feel very strongly that amendments and revisions to the Ship Mortgage Act are going to be of considerable benefit not only to the marine lending community but certainly to the recreational boater. We have experienced a dramatic increase in waterfront development throughout this entire country. That waterfront development is obviously destined to increase the numbers of recreational boats that are sold. More boats will be sold when money is made more available to buy those boats. The more boats there are, the more recreational marine facilities are needed. The more those are needed, the more upgrading is done on waterfront property. Needless to say, this has helped the State treasuries. I appreciate the views on user fees, but there are various State-titling States that benefit a great deal when more boats are sold.

In summary, we are very appreciative to the Maritime Law Association's Marine Finance Committee, to the American Bar Association's Admiralty Committee, and certainly, to the Members of this Subcommittee to allow us to speak our piece. We stand ready in the months to come to assist you in any way possible to facilitate a clarification of the existing act. Thank you, sir.

Mr. JONES. Thank you, Mr. Theut.

Mr. King.

STATEMENT OF BRUCE A. KING, REPRESENTING THE SECTION OF BUSINESS LAW, AMERICAN BAR ASSOCIATION; C/O BOGLE & GATES, SEATTLE, WA

Mr. KING. Thank you, Mr. Chairman.

It is an honor to appear before this Subcommittee and have an opportunity to discuss the recodification of the Ship Mortgage Act.

If you please, I have submitted written testimony and would like merely to summarize that today.

Mr. JONES. Without objection, so ordered.

Mr. KING. I am a partner of the Seattle law firm of Bogle & Gates, where I specialize in maritime finance and regulation. I also serve as Vice-Chairman of the American Bar Association Subcommittee on Maritime Financing.

There was not time before the hearing to go through all of the Association's procedures to get official endorsement of my testimony today, so it is necessary for me to testify in my capacity as a private citizen and as a participant in the ABA subcommittee's efforts to propose substantive codification to the bill. When the ABA's approval is obtained, I will inform your Subcommittee by letter for the record.

The ABA Subcommittee has been working for three years on drafting proposed substantive revisions to the Ship Mortgage Act. Its aim has not been to totally restructure the system for perfecting security in vessels but, principally, has been to make it easier and cheaper to use, to clarify some of the ambiguities in the legislation, and also to correct some anomalies in it.

There are many antiquated and cumbersome procedures that the current Ship Mortgage Act requires. There is the use of affidavits of good faith, which have already been mentioned today. There are requirements that call for executing and submitting documents to the United States Coast Guard in a special sequence that only serves to increase the cost in closing transactions. This increase is a cost to the Government because it is the Coast Guard that is charged with the duty of processing these documents. It also increases the cost to the shipowners who, in typical transactions, are required to pay the lender's transactions costs.

In my experience, these additional hoops that it is necessary to go through to close these transactions can often add as much as one-third to the customshouse brokers' and attorneys' fees that are incurred in them. While we often usually think merely of large vessels when we deal with the Ship Mortgage Act, we should remember that around the country most vessel owners are small businessmen—typically, fishermen and tug and barge operators—and yacht owners for whom these are significant costs. These are individuals who find that the technical requirements of the legislation and the high costs that are involved in complying with it are often bewildering and infuriating.

In addition, this is inconvenient for the lending community because there are a number of modern financing techniques which are effectively unavailable in maritime financing. It is not possible under the current Act, for example, to use a mortgage subordination agreement in which one lienholder agrees that his rights will be junior to another's and to record this with the Coast Guard.

It is difficult to make provisions in loan agreements for shipowners to borrow and repay funds in a variety of foreign currencies. This is becoming increasingly common, since at least in the fishing industry in the northwest there has been a flight of U.S. lenders who are willing to finance the industry. It has become increasingly necessary to turn to Europe for capital in this industry.

Also, it is not possible to use what are commonly called "finance leases," which are very common security devices in land-based transactions.

Lastly, due to its complicated nature the current Act has a number of traps for the unwary. A lender and counsel who are not thoroughly versed in the intricacies of the Ship Mortgage Act can often find themselves making devastating mistakes that at first would appear to be of a rather trivial nature.

There is another problem that needs to be addressed. That concerns the tremendous backlog in processing yacht financing transactions that Mr. Theut just mentioned. In the last several years, the Coast Guard has made tremendous efforts to streamline its documentation procedures in its offices in an effort to deal with this backlog. Despite this, in many offices there are delays of up to three to six months in processing yacht transactions. Fortunately, the Coast Guard has given precedence to processing documentation for commercial vessels so that commerce isn't interrupted. But it still leaves sizable portfolios of major yacht lenders effectively unsecured for many months. This is dangerous for them.

Several solutions to this come to mind. One would be to increase the appropriations to the Coast Guard so that it can deal with the volume of paperwork that descends on it.

A second would be to dramatically simplify the documentation requirements under the Ship Mortgage Act, perhaps making them as simple as filing a financing statement under the Uniform Commercial Code in nonmaritime equipment financing transactions.

A third would be to adopt something on the line of Congressman Davis's proposal last year, that of shifting yacht documentation and mortgage transactions to the States.

I should like to point out that these three approaches are not mutually exclusive. All can be made to work, or any one could be made to work. Whatever is adopted, however, three considerations need to be borne in mind in adopting a solution.

Under current law, it would be possible for a yacht owner to title a vessel at the State level and grant a State law security interest in a yacht as security for a loan. At the same time, and without telling the first lender, it would be possible for this yacht owner to document the vessel with the Coast Guard, borrow money from a second lender, and grant the second lender a preferred mortgage. This is an obvious invitation to fraud, although I should say that I haven't seen too many instances where this has occurred. But as long as the question of dealing with security in vessels is before this Subcommittee, it would be a good opportunity to eliminate this opportunity to commit fraud.

In addition, if the documentation of yachts is left completely to the States, we need to give some attention to the question of how these yacht owners enter and clear customs in foreign countries when they take foreign cruises. As we know, very often these yachts are quite large, and people do like to take round-the-world cruises. They often have difficulty entering and clearing customs in Hong Kong, Borneo, or the like when they present a certificate of title from, say, the State of Oregon or the State of Texas. The certificate of title may not even have the words "United States of America" on it. These people often have a lot of explaining to do to get in and out of foreign countries.

Two solutions to this problem suggest themselves. One is to allow the States that document vessels to issue a document that says "United States of America, issued by authority by the State of Oregon," or something of that sort. Another is to allow the owner of a State-documented vessel to apply to the Coast Guard for a certificate of nationality of some sort that could be used to enter and clear customs in foreign countries.

A third issue needs to be borne in mind in dealing with yachts and in considering any substantive changes to the Ship Mortgage

Act. It is necessary to make certain that foreign courts that foreclose mortgages abroad on American vessels will give recognition to the security interests in them that we create. Our lenders need to know that their vessels can be arrested anywhere in the world and that their mortgages will be honored.

In the few moments that remain, I would like to discuss briefly some of the suggested revisions in the ABA's current draft. This draft was provided to your staff at its request last April. It is an ongoing project of our committee which will be meeting again in Toronto in August of this year. Most of the suggestions that have been dropped both by the ABA Subcommittee and by other groups we've heard from today are completely independent in nature. If any of them turn out to be controversial or unworkable, for the most part they can be discarded without affecting the viability of the other proposals.

The ABA draft has made the same suggestion that was advanced by the Coast Guard and the Maritime Law Association, that of permitting mortgages to be granted prior to the documentation of the mortgaged vessels.

In addition, the ABA draft allows the option of filing what would be called a notice of mortgage, which is very similar to the financing statement used under the Uniform Commercial Code. It would have a minimum of information on it that would be required: the name of the shipowner; the name of the mortgagee; the address of the mortgagee; the amount of the mortgage; and a description of the vessel. The document would be signed by the shipowner. This could be filed with the Coast Guard and would be deemed sufficient by statute to perfect a mortgage.

A side benefit of this, however, would be that the lenders would have the option, as always, of filing the complete mortgage instrument. The ABA draft provides that a mortgage would be deemed sufficient if the foregoing five items of information were on it. It would not be necessary for the Coast Guard to review the complete text of a mortgage to see if it complied with all of the provisions of the Ship Mortgage Act. If those five items of information were present, the documentation officer could simply record the mortgage, thus saving the Coast Guard a great deal of time.

The ABA draft would eliminate the affidavit of good faith and provide that the use of notarial acknowledgments be made optional.

The ABA draft also suggests that we clarify that there is a principle that compliance with the Ship Mortgage Act's requirement is sufficient if there has been substantial compliance, so that we do not encourage courts to adopt hypertechnical readings of the requirements of the Act.

The ABA draft also includes a proposal similar to that suggested by Mr. Barnett today, that mortgage trustees for foreign lenders be permitted to purchase vessels at judicial sales provided they purchase for resale only.

The ABA draft also adopts a suggestion from the Gilmore and Black treatise on maritime law. It suggests giving a measure of protection to the financial institutions which finance the acquisition of small items of equipment on vessels, such as radios and radar sets. A lender who has a purchase money security interest in, say, a radio, would be given priority over ship mortgages provided the radio could be readily removed without damage to the vessel. It was the sense of the ABA Subcommittee that this wasn't a major concession by the mortgage lenders but, in fact, might eliminate much lien priority litigation over very small and insignificant pieces of equipment. In my own experience, when the question of radios and things of that sort comes up in litigation, the litigation costs can exceed the value of the piece of equipment at issue. I would suggest a clear statement of priority principles on those devices in an effort to minimize litigation costs.

I appreciate this opportunity to make my views known today.

[The prepared statement of Mr. King can be found at the end of the hearing.]

Mr. JONES. Thank you, Mr. King.

Our next witness is John C. Moriniere.

STATEMENT OF JOHN C. MORINIERE, GENERAL MANAGER, OILTOOLS DIVISION, STEWART & STEVENSON SERVICES, INC., HOUSTON, TX

Mr. MORINIERE. Mr. Chairman, and Members of the Subcommittee, I am John C. Moriniere, General Manager of the Oiltools Division of Stewart & Stevenson Services, Inc. headquartered in Houston. I thank you for the opportunity to appear before you today and discuss a matter of concern for our company and others.

In one area of our business, we provide services to financial institutions who have provided financing for U.S.-flag vessels. In this capacity we have become aware of an interpretation problem with the Ship Mortgage Act of 1920. Foreign banks participating in financing U.S.-flag vessels must, in order to obtain a preferred mortgage, use an approved trustee which is a U.S. citizen. The trustee will hold the mortgage in its name in a trust for the benefit of the noncitizen foreign bank or bank syndicate. This type of trust is today referred to as Westhampton Trust.

The name Westhampton Trust arose from the case of *Chemical Bank of New York Trust Co.* v. *S.S. Westhampton,* 358 F.2d 574 (4th Cir. 1965) and the Westhampton Amendments to the Ship Mortgage Act adopted as a result of that case by Congress in 1965 (Public Law 89-346). In that case the trustee was a U.S. citizen bank which had issued a bond to the beneficiary of the trust, a noncitizen foreign bank. In determining whether the mortgage on the U.S.-flag vessel to the trustee/mortgagee, which secured the note to the noncitizen bank, was a valid mortgage under the Ship Mortgage Act, the court did not question the U.S. citizenship of the bank mortgagee, which must be a U.S. citizen for the mortgage to be preferred, but struck down the preferred status of the mortgage on the ground that the issuance of the note to the foreign bank was a transfer of an interest in the vessel which was the subject of the mortgage, which transfer had not been approved by the Secretary under section 9 of the Shipping Act, 1916, as amended. Congress quickly amended Subsection 0 of the Ship Mortgage Act by adding subsection (e) which allows the issuance and transfer of such notes or bonds secured by a mortgage of a vessel to a trustee meeting certain conditions and approved by the Secretary. Thus, the courts and the Congress have treated an approved trustee as a U.S. citizen.

Over the past eight years, the Westhampton Trust has been used to provide approximately $2 billion of financing for U.S.-flag vessels with participation by more than 25 foreign financial institutions. These numbers do not take into account financing for numerous pleasure craft presently documented in this country.

The U.S. Justice Department and the Maritime Administration have interpreted the Ship Mortgage Act regarding one essential element of a mortgagee's rights in such a way that, whereas an approved trustee is a citizen for the purpose of having its mortgage considered as a preferred mortgage, it is not a citizen for the purpose of exercising the essential remedy of bidding for the vessel at a judicial sale in the United States.

The ability of the trustee-mortgagee to bid at such a judicial sale is necessary to protect its beneficiary from a sale of the vessel at less than the indebtedness or the true value, particularly in a depressed market.

Although in a judicial sale a vessel is free and clear from all preexisting claims, which is a distinct advantage, such judicial sale is not conducive to obtaining the best price for the vessel. However, purchase of a vessel free and clear of preexisting claims by the trustee at a judicial sale followed in time by a private sale should insure the greatest protection to the beneficiary.

The trustee needs only the ability to bid and purchase the vessel at a judicial sale—subject to the trust—and resell that vessel. The trustee does not need to be able to document the vessel, operate the vessel, or take any other action with respect to that vessel which would require any modifications of the existing law.

The purpose of the proposed change is not to give the approved trustee, acting pursuant to its trust for a foreign financial institution, any greater, or even equal, rights than a U.S. citizen financial institution has. The effect of the proposed amendment would be only to permit the approved trustee to purchase the vessel subject to the mortgage held in trust at a judicial sale and to hold the vessel for resale.

After confirmation of the sale, the U.S. Coast Guard Documentation Office would be advised that the trustee was the successful bidder, and the vessel would be deleted from documentation. In all other respects, existing law would remain unchanged.

Upon resale by the trustee, the vessel will be redocumented in the name of the new owner, if a U.S. citizen. If the subsequent sale is to a person who is not a U.S. citizen, a request will be made of the Secretary of Transportation, through the submittal of a Form MA–29, for approval of transfer of ownership, registry, and flag or charter, lease or mortgage of a U.S. citizen-owned and -documented vessel to the new non-U.S. citizen owner.

However, the proposed amendment would make it clear that without the approval of the Secretary the trustee may not: (1) sell, mortgage, lease, charter, deliver, or in any manner transfer to any noncitizen or place under foreign registry the vessel or any interest thereon; and (2) operate the vessel. The vessel, when owned by the trustee, is subject to the provisions of the Merchant Marine Act, 1936, as amended, with regard to requisitioning, purchasing, or chartering the vessel during any national emergency.

The issue of loss of coastwise trading privileges due to the trustee's becoming the owner for the sole purpose of reselling the vessel should be treated the same as a transfer to a U.S. corporation whose stock may be 100 percent owned by a noncitizen, commonly known as a documentation citizen. In such a case, the Coast Guard regulations do not treat this as a sale "foreign." Such a transfer does not preclude a U.S.-flag vessel from participating in coastwise trade upon redocumentation.

We have worked with Committee staff on wording to correct this problem. In our opinion, we think that the current proposed wording will be beneficial to all parties. We encourage passage of the wording in H.R. 3105.

I would like to thank all members of the staff for working with me and being so helpful. We would be glad to answer any questions you may have. Thank you.

Mr. JONES. Thank you, Mr. Moriniere. There are some questions which Congressman Davis will submit for the record. Without objection, so ordered.

Mr. King and Mr. Theut, the Maritime Law Association made a number of recommendations for substantive changes in the law. Give us your view of each of these recommendations.

Mr. THEUT. With respect to substantive changes, the ones that the National Marine Bankers Association would endorse are as follows:

Number one: Any change that would facilitate the mortgage being effected upon filing.

Number two: The notice of mortgage provision. In other words, some sort of a notice that could be filed by a marine lender that would indicate that when the money is loaned there at least is some notice on the record that that money is outstanding; that there is a security interest out; that the owner of the vessel recognizes that the vessel is about to be documented; and that the owner of the vessel would not be able to unilaterally stop the documentation procedure without knowledge of the lender. All of that sort of thing, Mr. Chairman, would be covered in a notice of mortgage provision. That would be the second substantive change we would endorse.

Number three: We also certainly would endorse any change that would eliminate the affidavit of good faith. I mentioned one of the cases that we have been very concerned about on the West Coast that did involve the interpretation of an affidavit of good faith. We would like that area clarified. We would not shed any tears if that were eliminated.

Number four: Any change that would codify the substantial compliance doctrine. That is a very aged maritime law doctrine. The greatest danger in a first preferred ship mortgage is the fact that, if someone can find a very minor technical defect, it obviously could be destroyed. It would lose its preferred status. Under the substantive compliance doctrine, you get away from some of that "nitpicking." We would very much endorse that.

Number five: Mr. King's comment on the purchase money mortgage provision. There is a tremendous market out there for the recreational boater on after-acquired property. I think that marine lenders would be much more amenable to putting a package together for the recreational boater if they were aware where the purchase money mortgage on that equipment comes priority-wise with reference to the first preferred ship mortgage.

So, Mr. Chairman, those five substantive changes we would heartily endorse.

Mr. JONES. Mr. King, do you care to address that briefly?

Mr. KING. Yes, Mr. Chairman.

The current ABA draft has actually retained the requirement of endorsement of a preferred mortgage. I should say, however, that in our various meetings over the last couple of years the Subcommittee has gone back and forth on the issue, so that probably should not be taken as a final statement of position. We will be taking this up at our next meeting in Toronto. I wouldn't be surprised if the ABA subcommittee got on board with the Maritime Law Association and the Coast Guard on that point.

The ABA's draft already suggests dropping the affidavit of good faith and the provision concerning stipulations that the mortgagees not waive their preferred status.

We will be taking up at our meeting in Toronto the Maritime Law Association's suggested language concerning the amount of the mortgage. I would personally agree that something along the lines suggested by Mr. Barnett is in order. It is one of the areas that causes the most problems in trying to tailor the requirements of the Ship Mortgage Act to some modern financing devices.

With respect to the proposal permitting Westhampton trustees to bid at judicial sales, the ABA draft provision is slightly broader than the Maritime Law Association's provision. Under current financing practice, the Westhampton trustee always holds the preferred mortgage for the alien lender. Occasionally, however, the transactions are structured so that the promissory note, the actual instrument of indebtedness, is also held by the trustee, with the thought that it is somewhat anomalous to have the debt held by one party and the mortgage held by another.

The Maritime Law Association's suggested language would restrict the ability of a Westhampton trustee to bid and obtain the mortgaged vessel at the foreclosure sale to instances where the trustee holds the mortgage but not the promissory note. I can't see any reason in principle to distinguish the two situations. That is discussed further in paragraph 14 of my written testimony.

Mr. JONES. Thank you, Mr. King.

Turnabout is fair play now. Mr. Barnett and Mr. Theut, what are your opinions on each of the recommendations made by Mr. King?

Mr. BARNETT. Mr. Chairman, I think that the MLA recommendations and Mr. King's recommendations, to a rather satisfying extent, cover much of the same ground, particularly the emphasis on getting rid of these unnecessary and obsolete technical requirements that are in the Ship Mortgage Act.

Some of the other suggestions that have been made with respect to the Westhampton trustee situation are largely a matter of working out language that is satisfactory to all parties. So I think we have tried to strike a balance here between trying to do a number changes in the Ship Mortgage Act and, on the other hand, recognizing that at this time there are limitations on what can be done if this Act is to go forward, which we want it to do. So, I think that there is a large area of agreement between our recommendation and those of Mr. King.

Mr. THEUT. Mr. Chairman, I certainly would agree with that, and certainly the five substantive changes outlined a moment ago. Many of those are contained in Mr. King's draft.

Philosophically speaking, the National Marine Bankers Association wants very much to keep the Ship Mortgage Act strong and viable. Our problem really comes at the other end of the line. That is, what do we do about those vessels that are not documentable. That is not a problem that this Committee is particularly addressing, but that is a problem very severe to us.

A couple of things that Mr. King mentioned, I think, must be preserved. That is the so-called convenience that the Ship Mortgage Act has allowed American vessels throughout the years. We are dealing here with an Act that was initially designed for U.S. warships. It obviously has now come down to rather small vessels. But there still is a very good thing about that Act in the sense that it does enable our citizens to go rather easily between Canada and certainly European countries. I think it is very important that that aspect of the Act be kept.

Also, the current situation, Mr. Chairman, for fraud that Mr. King mentioned, is obviously something that is of great concern to us. As long as we have dual titling systems in this country, we are going to occasionally have people who perpetrate tremendous frauds in financing vessels. I would just say this, then, on behalf of the National Marine Bankers Association. Fraud perpetrated by borrowers is not translated into any significant dollar amount; but when one of those fraud cases happens every 5 years or so, it probably knocks about 10 major lenders out of the market for another 3 years. So, the dollar amount isn't that big directly, but the indirect impact of a fraud in the marine lending industry kind of spreads and dampers enthusiasm for lending.

Mr. JONES. Thank you.

Why can't the condition to allow mortgages to be paid off in foreign currency be made a part of the provisions of a mortgage between the interested parties? In other words, why must this be legislated? Does anyone have an opinion?

Mr. BARNETT. I think the present Coast Guard regulations do attempt to deal with the problem to some extent. The Liberian maritime law, which was originally based on the United States law, has been amended to deal with these multi-currency options and other financing techniques. I believe it would increase the feeling of certainty that lenders would have in the validity of their security instruments if these multi-currency options and loans in foreign currencies were given recognition in the legislation and not just left to agreement between the parties.

Mr. JONES. Thank you.

Finally, Mr. Moriniere, would you comment on the MARAD proposals to limit trustee mortgage purchase for resale only?

Mr. MORINIERE. I don't think I am prepared to comment on that. I might defer to Mr. Barnett.

Mr. **Barnett**. I think that providing that the trustee must hold the vessel for resale purposes only certainly limits the flexibility of the lender in recovering on its investment. It may be in the lender's interest to charter the vessel out for a period of time and to attempt to recover something on its investment in that way. So from the point of view of lenders, this limitation is a restriction which is to some extent burdensome. But I think that the ship financing industry and foreign lenders would be quite prepared to live with that limitation if that is what is necessary in order to get the legislation passed.

Mr. **Jones**. Thank you.

Mr. Moriniere.

Mr. **Moriniere**. I might just add that I don't think that is a problem in talking to numerous lenders. I think that if we are limited to the fact that the vessel can only be held subject to resale, that that's not a problem.

Mr. **Jones**. Thank you.

We thank you gentlemen for your presence here this morning.

The Chair would like to note that the Gentleman from Kentucky, Mr. Hubbard, is now in attendance.

There will be no further business. The Subcommittee stands adjourned.

[Whereupon, at 11:30 a.m., the Subcommittee was adjourned.]

[The following was submitted for the record:]

I

100TH CONGRESS
1ST SESSION

H. R. 3105

To revise, consolidate, and enact certain laws related to maritime commercial instruments and liens and public vessels and goods as chapters 313 and 315 of title 46, United States Code, "Shipping".

IN THE HOUSE OF REPRESENTATIVES

AUGUST 5, 1987

Mr. JONES of North Carolina (for himself, Mr. BIAGGI, Mr. ANDERSON, Mr. DAVIS of Michigan, and Mr. LENT) introduced the following bill; which was referred to the Committee on Merchant Marine and Fisheries

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A BILL

To revise, consolidate, and enact certain laws related to maritime commercial instruments and liens and public vessels and goods as chapters 313 and 315 of title 46, United States Code, "Shipping".

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

CHAPTERS 313 AND 315 OF TITLE 46, UNITED STATES CODE

SECTION 1. (a) Certain general and permanent laws of the United States, related to maritime commercial instruments and liens and public vessels and goods, are revised, consolidated, and enacted by subsection (b) of this section as chapters 313 and 315 of title 46, United States Code, "Shipping".

(b) Subtitle III of title 46, United States Code, is amended by striking out at the end—

"[CHAPTERS 313, 315—RESERVED]"

and substituting the following:

"CHAPTER 313—COMMERCIAL INSTRUMENTS AND MARITIME LIENS

"SUBCHAPTER I—GENERAL

"Sec.
"31301. Definitions.
"31302. Availability of instruments, prescribing fees, and acknowledgment requirement.
"31303. Certain civil actions not authorized.
"31304. Liability for non-compliance.
"31305. Waiver of lien rights.
"31306. Rules of law not affected.
"31307. Regulations.

"SUBCHAPTER II—COMMERCIAL INSTRUMENTS

"31321. Recording and discharge.
"31322. Preferred mortgages.
"31323. Disclosing and incurring obligations before executing preferred mortgages.
"31324. Retention and examination of mortgages and documents of self-propelled vessels covered by preferred mortgages.
"31325. Preferred mortgage liens and enforcement.
"31326. Court sales to enforce preferred mortgage liens and priority of claims.
"31327. Surrender of documents of preferred mortgage vessels.
"31328. Forfeiture of mortgagee interest.
"31329. Limitations on providing mortgaged vessel interests to persons not citizens.
"31330. Penalty.

"SUBCHAPTER III—MARITIME LIENS

"31341. Persons presumed to have authority to procure necessaries.
"31342. Establishing maritime liens and enforcement.
"31343. Recording and discharging liens on preferred mortgage vessels.
"31344. Court sales to enforce maritime liens.
"31345. State statutes superseded.

"SUBCHAPTER I—GENERAL

"§ 31301. Definitions

"In this chapter—

"(1) 'documented vessel' means a vessel for which a certificate of documentation has been issued under chapter 121 of this title.

"(2) 'mortgagee', when a mortgage on a vessel involves a trust deed and a bond issued under the deed, means the trustee designated in the deed.

"(3) 'necessaries' for a vessel includes repairs, supplies, and towage of the vessel and the use of dry dock and marine railway for the vessel.

"(4) 'preferred maritime lien' means a lien on a vessel—

"(A) arising before a preferred mortgage was recorded and endorsed under sections 31321 and 31322 of this title;

"(B) for damages arising out of maritime tort;

"(C) for wages of a stevedore when employed directly by a person listed in section 31341 of this title;

"(D) for wages of the crew of the vessel;

"(E) for general average; and

"(F) for salvage, including contract salvage.

"(5) 'preferred mortgage'—

"(A) means a mortgage that is a preferred mortgage under section 31322 of this title; and

"(B) also means in sections 31325 and 31326 of this title, a mortgage, hypothecation, or similar charge that is security on a documented foreign vessel (except any of the following vessels of less than 200 gross tons: a towing vessel, barge, scow, lighter, car float, canal vessel, or tank vessel) if the mortgage was executed under the laws of the foreign country under whose laws the vessel is documented and has been registered under those laws in a public register at the port of registry of the vessel or at a central office.

"(6) 'Secretary' means the head of the department in which the Coast Guard is operating.

"§ 31302. Availability of instruments, prescribing fees, and acknowledgment requirement

"(a) An instrument recorded with the Secretary under this chapter is available for public inspection.

"(b) On request, the Secretary shall provide a copy, including a certified copy, of an instrument recorded under this chapter.

"(c) The Secretary may prescribe reasonable fees for recording instruments and providing copies under this chapter.

"(d) An instrument to be recorded under section 31321 or 31343 of this title must be acknowledged before a notary public or other official authorized by a law of the United States or of a State to acknowledge deeds.

"§ 31303. Certain civil actions not authorized

"If a mortgage covers a vessel and additional property that is not a vessel, this chapter does not authorize a civil action in rem in admiralty to enforce the rights of the mortgagee under the mortgage against the additional property.

"§ 31304. Liability for non-compliance

"(a) If a person makes a contract secured by, or on the credit of, a documented vessel covered by a preferred mortgage and sustains a loss because—

"(1) the Secretary did not comply with a requirement imposed on the Secretary under this chapter, the United States Government is liable for the loss; or

"(2) the mortgagor or the master or other individual in charge of the vessel does not comply with a requirement imposed on the mortgagor, master, or individual under this chapter, the mortgagor is liable for the loss.

"(b) A civil action may be brought to recover for losses referred to in subsection (a) of this section. The district courts of the United States have original jurisdiction of the action, regardless of the amount in controversy or the citizenship of the parties. If the plaintiff prevails, the court shall award costs and an attorney's fee to the plaintiff.

"§ 31305. Waiver of lien rights

"This chapter does not prevent a mortgagee or a person performing or supplying necessaries from waiving at any time by agreement or otherwise the mortgagee's or person's right to a lien or, if a preferred mortgage lien, to the preferred status of the lien.

"§ 31306. Rules of law not affected

"This chapter does not affect the rules of law in existence on June 5, 1920, about—

"(1) the right to proceed against a vessel for advances;

"(2) laches in enforcing liens on a vessel;

"(3) the right to proceed in personam;

"(4) the rank of preferred maritime liens among themselves; and

"(5) priorities between maritime liens and mortgages (except preferred mortgages) on vessels of the United States.

"§ 31307. Regulations

"The Secretary may prescribe regulations, about recording and endorsing bills of sales, conveyances, mortgages, and assignments of vessels of the United States, that the Secretary considers necessary in carrying out this chapter.

"SUBCHAPTER II—COMMERCIAL INSTRUMENTS

"§ 31321. Recording and discharge

"(a) A bill of sale, conveyance, mortgage, or assignment of a mortgage that includes any part of a documented vessel must be recorded with the Secretary to be valid, to the extent the vessel is involved, against any person except—

"(1) the grantor, mortgagor, or assignor;

"(2) the heir or devisee of the grantor, mortgagor, or assignor; and

"(3) a person having actual notice of that instrument.

"(b) To be recordable, a bill of sale, conveyance, mortgage, or assignment of a mortgage must—

"(1) state the interest of the grantor, mortgagor, or assignor in the vessel;

"(2) state the interest sold, conveyed, mortgaged, or assigned; and

"(3) be acknowledged.

"(c) The Secretary shall—

"(1) record the bills of sales, conveyances, mortgages, and assignments of mortgages complying with subsection (b) of this section in the order they are received for recordation; and

"(2) maintain indexes of those instruments of—

"(A) the names of the vessels;

"(B) the names of the parties to the instruments;

"(C) the time and date each instrument was received;

"(D) the interest in the vessel that was sold, conveyed, mortgaged, or assigned; and

"(E) if a mortgage, the amount and date of maturity of the mortgage.

"(d)(1) On discharging any part of the indebtedness under a mortgage recorded under this section, a mortgagor shall provide the Secretary with a written, acknowledged certificate of discharge of the indebtedness. The Secretary shall record the certificate.

"(2) If a vessel is covered by a preferred mortgage—

"(A) the Secretary shall endorse the discharge on the vessel's certificate of documentation; and

"(B) the Secretary of the Treasury may clear the vessel under section 4197 of the Revised Statutes (46 App. U.S.C. 91) only after the endorsement has been made.

"§ 31322. Preferred mortgages

"(a) A preferred mortgage is a mortgage that—

"(1) includes the whole of a documented vessel (except any of the following vessels of less than 25 gross tons: a towing vessel, barge, scow, lighter, car float, canal vessel, or tank vessel);

"(2) is recorded as provided by section 31321 of this title;

"(3) when applicable, complies with subsection (b) of this section;

"(4) is endorsed as provided by subsection (d) of this section;

"(5) is accompanied by an affidavit that the mortgage is made in good faith and without any design to hinder or defraud an existing or future creditor of the mortgagor or a lienor of the vessel;

"(6) does not stipulate that the mortgagee waives the mortgage's preferred status; and

"(7) has as the mortgagee—

"(A) a State;

"(B) an individual who is a citizen of the United States; or

"(C) a citizen of the United States described under the first section and section 2 of the Shipping Act, 1916 (46 App. U.S.C. 801, 802).

"(b) If a mortgage covers a vessel and additional property that is not a vessel, the mortgage may be a preferred mortgage only if the mortgage provides for the separate discharge of the additional property by paying a specified part of the mortgage indebtedness.

"(c) A preferred mortgage may have any rate of interest that the parties to the mortgage agree to.

"(d) The Secretary shall endorse the following on any certificate of documentation of a vessel to be covered by a preferred mortgage:

"(1) the name of the mortgagor.

"(2) the name of the mortgagee.

"(3) the time and date of the endorsement.

"(4) the amount of the mortgage.

"(5) the date of maturity.

"(6) the specified part of the mortgage indebtedness that has to be paid for the separate discharge of a vessel as provided under subsection (b) of this section.

"(7) if a mortgage covers more than one vessel and provides for the separate discharge of each vessel by paying a specified part of the mortgage indebtedness, the specified amount applicable to that vessel.

"(e) If a preferred mortgage covers more than one vessel without providing for the separate discharge of a vessel and is to be sold by order of a district court of the United States in a civil action in rem in admiralty, the amount of the mortgage indebtedness attributable to the vessel is that part of the indebtedness, increased by 20 percent, that the court determines approximates the value that the vessel bears to the value of all the vessels covered by the mortgage.

"(f) The Secretary of the Treasury may clear a vessel under section 4197 of the Revised Statutes (46 App. U.S.C. 91) only after the endorsements required by subsection (d) of this section have been made:

"§ 31323. Disclosing and incurring obligations before executing preferred mortgages

"(a) On request of the mortgagee and before executing a preferred mortgage, the mortgagor shall disclose in writing to the mortgagee the existence of any obligation known to the mortgagor on the vessel to be mortgaged.

"(b) After executing a preferred mortgage and before the mortgagee has had a reasonable time to record the mortgage and have endorsements about the mortgage put on the vessel's certificate of documentation, the mortgagor may not incur, without the consent of the mortgagee, any contractual obligation establishing a lien on the vessel except—

"(1) a lien for wages of a stevedore when employed directly by a person listed in section 31341 of this title.

"(2) wages for the crew of the vessel.

"(3) general average.

"(4) salvage, including contract salvage.

"(c) On conviction of a mortgagor under section 31330 of this title for violating this section, the mortgage indebtedness, at the option of the mortgagee, is payable immediately.

"§ 31324. Retention and examination of mortgages and documents of self-propelled vessels covered by preferred mortgages

"(a) A mortgagor of a preferred mortgage covering a self-propelled vessel shall use diligence in keeping a certified copy of the mortgage on the vessel.

"(b) On request, the owner, master, or individual in charge of a self-propelled vessel covered by a preferred mortgage shall permit a person to examine the mortgage and vessel's certificate of documentation if the person has business with the vessel that may give rise to a maritime lien or the sale, conveyance, mortgage, or assignment of a mortgage of the vessel.

"§ 31325. Preferred mortgage liens and enforcement

"(a) A preferred mortgage is a lien on the mortgaged vessel in the amount of the outstanding mortgage indebtedness secured by the vessel.

"(b) On default of any term of the preferred mortgage, the mortgagee may enforce the preferred mortgage lien in—

"(1) a civil action in rem in admiralty; or

"(2) a civil action in personam in admiralty against the mortgagor for the amount of the mortgage indebtedness secured by the mortgaged vessel or any deficiency in paying off that indebtedness.

"(c) The district courts of the United States have—

"(1) original jurisdiction, exclusive of the courts of the States, of a civil action brought under subsection (b)(1) of this section; and

"(2) original jurisdiction of an action brought under subsection (b)(2) of this section.

"(d)(1) Actual notice of a civil action brought under subsection (b)(1) of this section must be given in the manner directed by the court to—

"(A) the master or individual in charge of the vessel; and

"(B) any person that recorded under section 31343(a) of this title a notice of a claim of an undischarged lien on the vessel.

"(2) Notice under paragraph (1) of this subsection is not required if, after search satisfactory to the court, the person entitled to the notice is not found in the United States.

"(3) Failure to give notice required by this subsection does not affect the jurisdiction of the court in which the civil action is brought. However, when notice is not required under paragraph (2) of this subsection, the mortgagee is liable to the person not notified for damages in the amount of that person's interest in the vessel terminated by the action brought under subsection (b)(1) of this section. A civil action may be brought to recover the amount of the terminated interest. The district courts of the United States have original jurisdiction of the action, regardless of the amount in controversy or the citizenship of the parties. If the plaintiff prevails, the court shall award costs and an attorney's fee to the plaintiff.

"(e) In a civil action brought under subsection (b)(1) of this section—

"(1) the court may appoint a receiver and authorize the receiver to operate the mortgaged vessel; and

"(2) when directed by the court, a United States marshal may take possession of a mortgaged vessel even if the vessel is in the possession or under the control of a person claiming a possessory common law lien.

"§ 31326. Court sales to enforce preferred mortgage liens and priority of claims

"(a) When a mortgaged vessel is sold by order of a district court of the United States in a civil action brought under section 31325(b)(1) of this title, any prior claim in the vessel is terminated, including a possessory common law lien of which a person is deprived under section 31325(e)(2) of this title.

"(b) Each of the claims terminated under subsection (a) of this section attaches, in the same amount and priority, to the proceeds of the sale, except that—

"(1) the preferred mortgage lien has priority over all other claims against the vessel (except for expenses and fees allowed by the court, costs imposed by the court, and preferred maritime liens); and

"(2) for a foreign vessel, the preferred mortgage lien is subordinate to a maritime lien for necessaries performed or supplied for the vessel in the United States.

"§ 31327. Surrender of documents of preferred mortgage vessels

"Except when a vessel is forfeited or sold by order of a court of the United States or a foreign country, the certificate of documentation of a documented vessel covered by a preferred mortgage may be surrendered only with the approval of the Secretary. The Secretary may approve the surrender only if the mortgagee consents.

"§ 31328. Forfeiture of mortgagee interest

"The interest of a mortgagee in a mortgage covering a documented vessel may be terminated by a forfeiture of the vessel for a violation of a law of the United States only if the mortgagee authorized, consented, or conspired to do the act, failure, or omission that is the basis of the violation.

"§ 31329. Limitations on providing mortgaged vessel interests to persons not citizens

"(a) An evidence of indebtedness secured by a mortgage of a vessel to a trustee may be issued, assigned, or transferred to a person not a citizen of the United States only if the trustee is approved by the Secretary. The Secretary shall approve the trustee if the trustee is a bank or trust company that—

"(1) is a corporation and doing business under the laws of the United States or of a State;

"(2) is authorized to exercise corporate trust powers;

"(3) is a citizen of the United States;

"(4) is subject to supervision or examination by an official of the Government or a State; and

"(5) has a combined capital and surplus (as stated in its most recent published report of condition) of at least $3,000,000.

"(b) If the trustee at any time does not satisfy the qualifications of subsection (a) of this section, the Secretary shall disapprove the trustee.

"(c) A right under a mortgage of a documented vessel may be assigned to a person not a citizen of the United States only with the approval of the Secretary.

"(d) In a civil action in rem in admiralty, a documented vessel may be sold by order of a district court of the United States to a person not a citizen of the United States only with the approval of the Secretary.

"(e) The issuance, transfer, or assignment of an evidence of indebtedness contrary to this section is void.

"§ 31330. Penalty

"(a) A mortgagor shall be fined not more than $1,000, imprisoned for not more than 2 years, or both, if the mortgagor, with intent to defraud—

"(1) does not disclose an obligation on a vessel as required by section 31323(a) of this title; or

"(2) incurs a contractual obligation in violation of section 31323(b) of this title.

"(b) If the mortgagor is a corporation or association, the president or chief executive officer of the corporation or association also is liable as a mortgagor under this section.

"SUBCHAPTER III—MARITIME LIENS

"§ 31341. Persons presumed to have authority to procure necessaries

"(a) The following persons are presumed to have authority to procure necessaries for a vessel:

"(1) the owner.

"(2) the master.

"(3) a person entrusted with the management of the vessel at the port of supply.

"(4) an officer or agent appointed by—

"(A) the owner;

"(B) a charterer;

"(C) an owner pro hac vice; or

"(D) an agreed buyer in possession of the vessel.

"(b) A person improperly in possession or charge of a vessel has no authority to procure necessaries for the vessels.

"§ 31342. Establishing maritime liens and enforcement

"A person providing necessaries for a vessel, on the order of a person listed in section 31341 of this title or a person authorized by the owner—

"(1) has a maritime lien on the vessel;

"(2) may bring a civil action in rem in admiralty to enforce the lien; and

"(3) is not required to allege or prove in the action that credit was given to the vessel.

"§ 31343. Recording and discharging liens on preferred mortgage vessels

"(a) Any person claiming a lien on a vessel covered by a preferred mortgage may record with the Secretary a notice of that person's lien claim on the vessel. To be recordable, the notice must—

"(1) state the nature of the lien;

"(2) state the date the lien was established;

"(3) state the amount of the lien;

"(4) state the name and address of the person; and

"(5) be acknowledged.

"(b) The Secretary shall record the notices complying with subsection (a) of this section.

"(c) On discharging any part of the indebtedness that is the basis for a claim recorded under this section, the person having the claim shall provide the Secretary with a written, acknowledged certificate of discharge of the indebtedness. The Secretary shall record the certificate.

"§ 31344. Court sales to enforce maritime liens

"When a documented vessel covered by a preferred mortgage is sold by order of a district court of the United States to enforce a maritime lien (except a preferred maritime lien), the vessel shall be sold free of all prior claims. However, on request of the mortgagee, plaintiff, or intervenor, the court shall require the buyer to give, and the mortgagee to accept, a new mortgage on the vessel for a period of time equal to the time remaining under the original mortgage. To the extent practicable, the conditions of the new mortgage shall be the same as those of the original mortgage, and the new mortgage is subject to approval by the court. When a new mortgage is given, the mortgagee may not be paid from the proceeds of the sale, and the amount payable as the buying price shall be reduced by the amount of the new mortgage indebtedness.

“§ 31345. State statutes superseded

“This subchapter supersedes any State statute conferring a lien on a vessel to the extent the statute establishes a claim to be enforced by a civil action in rem in admiralty against the vessel for necessaries.

“CHAPTER 315—PUBLIC VESSELS AND GOODS

“SUBCHAPTER I—GENERAL

“Sec.
“31501. Definitions.
“31502. Applicable law.
“31503. Public vessels and goods taken by legal process.
“31504. Subpenaing public vessel officers and crewmembers.

“SUBCHAPTER II—ACTIONS AGAINST THE UNITED STATES GOVERNMENT

“31511. Authorization to bring actions.
“31512. Limitation on actions by nationals of foreign countries.
“31513. Time and place for claims and actions.
“31514. Service of process.
“31515. Security.
“31516. Defenses and remedies.
“31517. Settlements.
“31518. Judgments against the United States Government.
“31519. Taking of public vessels and goods in foreign countries.
“31520. Payment of judgments and settlements.
“31521. Appropriations to pay judgments and settlements.

“SUBCHAPTER III—ACTIONS BY THE UNITED STATES GOVERNMENT

“31531. Actions by the United States Government.
“31532. Counterclaims, cross-claims, and credits.
“31533. Amounts recovered by the United States Government.

“SUBCHAPTER I—GENERAL

“§ 31501. Definitions

“In this chapter—

“(1) ‘agency’ means a department, agency, or instrumentality of the United States Government.

“(2) ‘public vessel’ means a vessel owned, demise chartered, or operated by the Government.

“§ 31502. Applicable law

“(a) Except as provided in this section, a civil action under this chapter shall proceed and be decided according to the principles of law and rules of practice applicable in like cases between private persons.

“(b) A civil action brought under this chapter is without a jury (including an advisory jury).

“(c) A person bringing a civil action under this chapter may elect to have the action proceed according to the principles of an action in rem if an action in rem could have been maintained if the vessel or the goods had been owned or possessed by a private person. Electing to proceed in rem under this subsection does not preclude the person bringing the action from properly seeking relief in personam in the same action.

"§ 31503. Public vessels and goods taken by legal process

"(a) A public vessel or goods owned or possessed by the United States Government that are on a vessel may not be arrested, attached, garnished, or executed on by legal process in the United States.

"(b) If a vessel once was a public vessel, but is no longer a public vessel, and is then arrested, attached, garnished, or executed on by legal process in the United States because of a civil action arising from a time when the vessel was a public vessel, the vessel shall be released without bond or stipulation if the Attorney General assumes the liability of satisfying a judgment in the action. The action shall proceed against the Government under this chapter.

"§ 31504. Subpenaing public vessel officers and crewmembers

"An officer or a crewmember of a public vessel may be subpenaed in connection with a civil action under this chapter only with the consent of—

"(1) the head of the agency having control of the vessel at the time the subpena is issued; or

"(2) the master or commanding officer of the vessel at the time the subpena is issued.

"SUBCHAPTER II—ACTIONS AGAINST THE UNITED STATES GOVERNMENT

"§ 31511. Authorization to bring actions

"(a) A person may bring a civil action in personam under this chapter against the United States Government for damages if—

"(1) a civil action under the admiralty and maritime law of the United States could have been maintained if the Government were a private person; and

"(2) a claim has been presented as provided under section 31513(a)(1) of this title.

"(b) The amount of damages a person seeks in a civil action arising under this chapter may not be more than the damages the person sought in the claim the person presented under section 31513(a)(1) of this title arising out of the same incident.

"§ 31512. Limitation on actions by nationals of foreign countries

"A national of a foreign country may bring a civil action under section 31511 of this title only if the government of that foreign country would allow a national of the United States to bring an action in its courts under similar circumstances. This section does not apply to an individual lawfully admitted for permanent residence in the United States.

"§ 31513. Time and place for claims and actions

"(a) A civil action may be brought under this chapter only—

"(1) after 6 months from the time a claim is presented in writing to the head of the agency having control of the public vessel or the goods owned or possessed by the United States Government involved in the claim; and

"(2) within 3 years from the date the cause of action accrues.

"(b)(1) A civil action may be brought under this chapter in the district court of the United States for the district in which—

"(A) a person bringing the action resides;

"(B) a person bringing the action has a principal place of business; or

"(C) the vessel or goods that is the basis for the action is found.

"(2) If there is no district under paragraph (1) in which to bring the civil action, the action may be brought in any district court of the United States.

"(c) The district court of the United States in which an action is brought under this chapter may transfer that action as provided under section 1404 of title 28.

"§ 31514. Service of process

"(a) Within 30 days after filing a civil action under this chapter, the person bringing the action shall serve process on the United States Government by sending a copy of the complaint, by certified mail, to the United States attorney for the district in which the action is brought and to the Attorney General.

"(b) The person bringing the action shall file proof of the service and mail required under subsection (a) of this section with the clerk of the court.

"§ 31515. Security

"(a) The United States Government may not be required to give a bond or stipulation in a civil action under this chapter.

"(b) When a counterclaim or cross-claim in a civil action under section 31511 of this title is filed, the person against whom the counterclaim or cross-claim is brought shall give security as directed by the court for the claim set out in the counterclaim or cross-claim. Proceedings in the action are stayed until the security is given.

"§ 31516. Defenses and remedies

"(a) The United States Government may limit its liability and use any defense available to a private person.

"(b) An officer, employee, agent, or member of the uniformed services of the Government is not liable for an act or omission giving rise to a claim or civil action under this chapter.

"§ 31517. Settlements

"(a) The head of an agency with whom a claim is filed under section 31513(a)(1) of this title may compromise and settle the claim.

"(b) The head of an agency shall report to Congress at the end of each session of Congress any settlement made under this section.

"§ 31518. Judgments against the United States Government

"(a) A judgment against the United States Government may include—

"(1) costs of the action; and

"(2) if a money judgment, interest.

"(b) The interest rate on a judgment of a civil action under this chapter is the rate equal to the coupon issue yield equivalent (as determined by the Secretary of the Treasury) of the average accepted auction price for the last auction of 52-week United States Treasury bills settled immediately before the date of judgment.

"(c) Interest is awarded in a civil action under this chapter from the time the action is brought. This subsection does not apply if there is a contract expressly providing for paying interest.

"(d) A judgment in a civil action under this chapter is subject to appeal under the admiralty and maritime law of the United States.

"§ 31519. Taking of public vessels and goods in foreign countries

"(a)(1) If a public vessel or goods owned or possessed by the United States Government on a vessel are arrested, attached, garnished, or executed on by legal process in a foreign country, the Secretary of State (when asked by the Attorney General) may direct the consul for the Government nearest to the vessel or goods to—

"(A) claim the vessel or goods are immune from arrest, attachment, garnishment, or execution; and

"(B) pledge the credit of the Government to pay any judgment and costs that may be entered against the Government in the proceeding.

"(2) If an action is brought in a foreign country against the master or commanding officer of a public vessel for any cause arising from, or in connection with, the vessel or goods on the vessel, the Secretary of State (when asked by the Attorney General) may direct the consul for the Government nearest to the place where the action is brought to—

"(A) enter the appearance of the Government; and

"(B) pledge the credit of the Government to pay any judgment and costs that may be entered against it in the action.

"(3) If a vessel once was a public vessel, but is no longer a public vessel, and is then arrested, attached, garnished, or executed on by legal process in a foreign country because of an action arising from a time when the vessel was a public vessel, the Secretary of State (when asked by the Attorney General) may direct the consul for the Government nearest to the vessel to—

"(A) claim the vessel is immune from arrest, attachment, garnishment, or execution; and

"(B) pledge the credit of the Government to pay any judgment and costs that may be entered against the Government in the proceeding.

"(b) The Attorney General may—

"(1) arrange to carry out subsection (a) of this section with any person, whether in the United States or a foreign country; and

"(2) pledge the credit of the Government in carrying it out.

"(c) This section does not prejudice or preclude the Government from properly claiming immunity of a vessel or goods from foreign jurisdiction.

"§ 31520. Payment of judgments and settlements

"(a) The United States Government shall pay a final judgment or settlement under this chapter from an appropriation or fund available to pay judgments or settlements.

"(b) Payment may be made under this section only after a certified copy of the judgment or settlement is presented to the Government. If the judgment is one of a foreign court under section 31519 of this title, the judgment shall be accompanied by—

"(1) a certificate and seal of the United States consul claiming the vessel or goods; and

"(2) a certificate of the Secretary of State as to the consul's official capacity.

"§ 31521. Appropriations to pay judgments and settlements

"When an appropriation or fund is not available to pay a final judgment or settlement as provided under section 31520(a) of this title, necessary amounts are appropriated to pay—

"(1) final judgments against the United States Government in actions under this chapter; and

"(2) settlements agreed to under this chapter.

"SUBCHAPTER III—ACTIONS BY THE UNITED STATES GOVERNMENT

"§ 31531. Actions by the United States Government

"(a) The United States Government may bring a civil action as a private person may under the admiralty and maritime jurisdiction of the courts of the United States.

"(b) The Attorney General may compromise and settle a claim of the Government brought under this section.

"(c) The Attorney General shall report to Congress at the end of each session of Congress any settlement made under this section.

"§ 31532. Counterclaims, cross-claims, and credits

"If the Attorney General brings a civil action for the United States Government under the admiralty or maritime law of the United States, a person may act as if the action is being brought by a private person and file a counterclaim or a cross-claim, in personam, or claim a credit against the Government.

"§ 31533. Amounts recovered by the United States Government

"(a) Amounts recovered in an action under section 31531 of this title that are not for the benefit of the crew shall be deposited in the Treasury and credited to the agency that controls the vessel.

"(b) Amounts recovered in a civil action by the United States Government arising from, or in connection with, a public vessel or goods on the vessel shall be deposited in the Treasury and credited to the agency that controls the vessel or goods. The amounts shall reimburse the appropriation or fund that pays for the loss or damage giving rise to the cause of action.".

LEGISLATIVE PURPOSE AND CONSTRUCTION

SEC. 2. (a) A reference to a law replaced by this Act, including a reference in a regulation, order, or other law, is deemed to refer to the corresponding provision of this Act.

(b) An order, rule, or regulation in effect under a law replaced by this Act continues in effect under the corresponding provision of this Act until repealed, amended, or superseded.

(c) An action taken or an offense committed under a law replaced by this Act is deemed to have been taken or committed under the corresponding provision of this Act.

(d) An inference of legislative construction is not to be drawn by reason of the caption or catch line of a provision enacted by this Act.

(e) If a provision of this Act is held invalid, all valid provisions that are severable from the invalid provision remain in effect. If a provision of this Act is held invalid in any of its applications, the provision remains valid for all valid applications that are severable from any of the invalid applications.

(f) This Act and laws revised, consolidated, and enacted by this Act do not affect the rights, duties, and obligations of the United States Government under chapter 171 of title 28, United States Code.

REPEALS

SEC. 3. (a) The repeal of a law by this Act may not be construed as a legislative implication that the provision was or was not in effect before its repeal.

(b) The laws specified in the following schedule are repealed, except for the rights and duties and matured, penalties that were incurred, and proceedings that were begun, before the date of enactment of this Act:

Statutes at Large

Date	Chapter or Public Law	Section	Statutes at Large		United States Code	Section
			Volume	Page		
1920						
Mar. 9	95		41	525	46 App.	741-752
June 5	250	30	41	1000	46 App.	911-984

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Statutes at Large—Continued

Date	Chapter or Public Law	Section	Statutes at Large		United States Code	Section
			Volume	Page		
1925						
Feb. 16	235		43	947	46 App.	1011–1014
Mar. 3	428		43	1112	46 App.	781–790
1948						
June 19	526	(provisos)	62	496	46 App.	740 (provisos)

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June 27, 1988

MEMORANDUM

TO: Members, Subcommittee on Merchant Marine

FROM: Majority and Minority Staff

SUBJECT: Hearing on Chapter 313 of H.R. 3105, an act to revise, consolidate, and enact the Ship Mortgage Act, 1920. (Tuesday June 28, 1988 at 10:00 a.m.)

INTRODUCTION

In 1984 this Committee began recodifying all of the maritime laws contained in title 46 of the United States Code. This process began with the vessel inspection and seaman protection laws in the 98th Congress. In the 99th Congress the vessel load line and tonnage measurement laws were revised and recodified into title 46. H.R. 3105 continues that process by recodifying the Ship Mortgage Act, 1920. It also recodifies the Suits in Admiralty and Public Vessel Act, but these will not be considered at this time. While the bill as introduced proposes to make no substantive changes to law, a number of witnesses will propose substantive changes that they believe will make vessel financing and mortgage recordation processes easier and more in keeping with modern practices.

BACKGROUND

The Ship Mortgage Act, 1920 was written at a time when Congress wanted to see large amounts of capital invested in the U.S. merchant marine, both by the Government and by private investors. They wanted to encourage shipowners to borrow on the value of the vessel. However, they recognized that to make this an attractive investment both the interest of the Government and the private investor would need to be protected. This Act sets out the priorities of liens on vessels so that in the event of a vessel arrest, bankruptcy, or foreclosure, the vessel assets of the company will be allocated on a priority basis. In general, the order of priority is (1) preferred maritime liens; (2) the preferred mortgage; (3) all other maritime liens; and (4) all other contract liens.

The following liens may be considered 'preferred maritime liens' on a vessel:

(1) Any lien arising before the preferred mortgage was recorded.
(2) Any lien for damages arising out of maritime tort, such as personal injury.
(3) A lien by a stevedore for wages.
(4) A lien by a crewmember of a vessel for wages.
(5) A lien for general average (which arise from claims for jettisoning or damaging cargo in order to save the vessel).
(6) A lien for salvage.

A preferred mortgage is a mortgage on a documented vessel (except certain vessels of less than 25 gross tons) that --

(1) has, as the mortgagee, a State, an individual who is a citizen of the United States, or a citizen of the United States as defined in section 1 or 2 of the Shipping Act, 1916 (46 App. U.S.C. 801 or 802);
(2) is recorded with the Secretary of Transportation;
(3) is granted in good faith without any design to hinder or defraud any creditor or lienor of the vessel; and
(4) is endorsed on the vessel's certificate of documentation.

SUBSTANTIVE CHANGES

While H.R. 3105 proposes to make no substantive change to the Ship Mortgage Act, a number of proposals are going to be made to make substantive changes that are purported to be noncontrovertial.

The Maritime Law Association of the United States (MLA) has been studying H.R. 3105 for the past 2 years. They are going to make a number of recommendations for substantive changes that they believe will make vessel financing and mortgage recordation easier. Their recommendations are as follows:

1. Eliminate the requirement that a mortgage be endorsed on the vessel's documents. They believe that this unduly complicates the perfection process and serves no added purpose since the mortgage itself must be placed and retained on board the vessel and available to interested parties. In addition, this requirement is not mandated by most other countries.

2. Eliminate the requirement that an affidavit be filed with the record of the mortgage to the effect that the mortgage is made in good faith and without any design to hinder, delay, or defraud any existing or future creditor of the mortgagor and any lienor of the mortgaged vessel. The MLA believe this has become a meaningless time-consuming formality.

3. Eliminate the requirement that a mortgage not stipulate that the mortgagee waives the preferred status of the mortgage. They state that this requirement has resulted in the drafting of mortgages in such strict compliance with the statute that economic realities are often ignored.

4. Allow mortgages to be paid off in foreign currency. Also allow revolving credit loans where advances and repayments are made, with a limitation on the maximum amount outstanding under the obligation at any one time limited to a certain amount. The current law states the "amount...of the mortgage" must be endorsed upon the documents of the vessel. This requirement makes these modern financing practices very difficult.

5. Eliminate the requirement that upon the payment of part of the mortgage, the mortgagor must file a notice with the Coast Guard. This requirement has been virtually ignored and not enforced by the Coast Guard since it would require every mortgagor to notify them every month when a mortgage payment is received.

6. Eliminate the prohibition on a vessel that is sold by order of a district court from being sold to a person that is not a citizen of the United States. This prohibits a trustee acting on behalf of a non-citizen lender that has lent the mortgage money from bidding on a vessel at a judicial foreclosure sale. Therefore, since they cannot bid, the vessel may be sold for less than the mortgage amount, causing them to suffer a loss. An amendment has been proposed to allow the trustee to bid, but not to operate the vessel if they are the high bidder.

7. Give the High Court of American Samoa jurisdiction to hear cases brought under this Act. The current law gives original jurisdiction of all civil actions to the district courts of the United States. However, the U.S. possession of Samoa does not have a district court.

8. Clarify that the Coast Guard is obligated to make available for public inspection mortgages and other instruments received by it for recordation, and that instruments received by the Coast Guard and accepted for recordation shall be deemed recorded at the date of receipt and acceptance. This stems from a 1987 court case concerning Pasquale Alberto in which the court had to decide whether the lien of a ship mortgage properly filed with the Coast Guard more than 90 days before the ship mortgagor filed a bankruptcy petition may be defeated by the bankruptcy trustee because the Coast Guard did not record the ship mortgage until

after the bankruptcy petition was filed.

Substantive changes concerning recreational vessels under the Ship Mortgage Act are also going to be discussed. Under current law a vessel mortgage can be recorded with the Coast Guard if it is a documented vessel. In the 21 states that have titling systems for recreational vessels that mortgage can also be recorded with the State. There have been cases of fraud in which 2 mortgages have been taken out on a vessel, one recorded with the Coast Guard and one with the State. Some have proposed that if a vessel can be titled in a State, then there should be a prohibition on recording the vessel mortgage with the Coast Guard. This would stop this type of fraud. Also, it may greatly ease the burden on the Coast Guard in these states for vessel mortgage recordation.

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cc: Members, Committee on Merchant Marine and Fisheries

SOURCE: Committee on Merchant Marine and Fisheries
Committee Print, September 1987

SECTION-BY-SECTION COMPARISON OF H.R. 3105, RECODIFICATION OF MARITIME LAWS

Revised Section	Source
31301(1)	46:911(1), (2), (4).
31301(2)	46:911(5).
31301(3)	Based on 46:971-974.
31301(4)	46:953(a).
31301(5)(A)	46:922(b).
31301(5)(B)	46:951 (2d par. less proviso).
31301(6)	New.
31302	46:926(b).
	46:927.
31303	46:954(b).
31304	46:941(c).
31305	46:974.
31306	46:974.
31307	46:983.
31321	46:921.
	46:925(b).
	46:926(a), (b).
	46:974.
31322	46:922.
	46:926(d).
31323	46:924.
	46:941(b) (last sentence).
31324	46:923.
31325	46:951 (1st par.).
	46:952.
	46:954(a).
31326	46:953(b).
	46:951 (2d par. proviso).
31327	46:961(a).
31328	46:961(b)
31329	46:961(d), (e), (f).
31330	46:941(b) (1st sentence).
31341	46:972.
	46:973.
31342	46:971.
	46:974.
31343	46:925(a).
	46:926(b).
31344	46:961(c).
31345	46:975.
31501	New.
31502(a)	46:743 (1st sentence).
	46:782 (last sentence words before 2nd comma).
31502(b)	46:742
31502(c)	46:743 (5th sentence).
	46:782 (last sentence words before 2nd comma).
31503(a)	46:741 (less proviso).
	46:788.
31503(b)	46:744.
31504	46:784.
31511	46:742 (1st sentence).
	46:781.

Revised Section	Source
31512	46:785.
31513(a)(1)	46:740 (last proviso).
31513(a)(2)	46:745 (words before 1st proviso).
31513(b)	46:742 (2nd sentence). 46:782 (1st sentence before semicolon).
31513(c)	46:782 (1st sentence after semicolon).
31513(d)	46:742 (last sentence).
31513(general)	46:782 (last sentence words before 2nd comma).
31514	46:742 (3rd sentence). 46:782 (last sentence words before 2nd comma).
31515(a)	46:743 (last sentence).
31515(b)	46:783 (proviso).
31515 (general)	46:782 (last sentence words before 2nd comma).
31516(a)	46:746. 46:789.
31516(b)	46:745 (1st proviso). 46:782 (last sentence words before 2nd comma).
31517(a)	46:749. 46:786.
31517(b)	46:752. 46:790.
31518(a)	46:743 (2nd sentence, 1st 24 words). 46:782 (last sentence words before 2nd comma).
31518(b)	46:743 (2nd sentence, 25th-last words). 46:782 (last sentence words before 2nd comma).
31518(c)	46:743 (3rd sentence). 46:745 (last proviso). 46:782 (last sentence words after 2nd comma).
31518(d)	46:743 (4th sentence). 46:782 (last sentence words before 2nd comma).
31519(a)(1)	46:747 (1st, 2nd sentences related to vessel and cargo).
31519(a)(2)	46:747 (1st, 2nd sentences related to master).
31519(b)	46:747.
31519(c)	46:747 (last sentence proviso).
31520(a)	46:747 (last sentence words before proviso). 46:748 (words between 4th and 5th commas). 46:787 (less words between 2nd–3rd commas).
31520(b)	46:748 (less words between 4th and 5th commas and words after semicolon). 46:787 (words between 2nd–3rd commas).
31521	46:748 (words after semicolon).
31531(a)	46:750 (words before 3rd comma).
31531(b)	46:749.
31531(c)	46:752.
31532	46:742 (5th sentence). 46:783 (words before proviso).
31533(a)	46:750 (words after 3rd comma).
31533(b)	46:751.

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SECTION-BY-SECTION ANALYSIS
OF H.R. 3105 --
TO REVISE, CONSOLIDATE, AND ENACT CERTAIN LAWS RELATED TO MARITIME COMMERCIAL INSTRUMENTS AND LIENS AND PUBLIC VESSELS AND GOODS AS CHAPTERS 313 AND 315 OF TITLE 46, UNITED STATES CODE

Section 1

Section 1 of H.R. 3105 revises, consolidates, and enacts certain general and permanent laws of the United States related to commercial instruments and liens and public vessels and goods. It amends subtitle III of title 46, United States Code by striking at the end "Chapters 313, 315 -- Reserved" and substituting "Chapter 313 -- Commercial Instruments and Maritime Liens". Chapter 313 is essentially a codification of the Ship Mortgage Act, 1920 (46 App. U.S.C. 911-984). Chapter 315 is a merger of the Suits in Admiralty Act (46 App. U.S.C. 741-752) and the Public Vessels Act (46 App. U.S.C. 781 et seq.), and will not be considered at this time. H.R. 3105 is the second step in the process of enacting laws compiled in title 46 of the Code into positive law. The first step in the codification process began in 1983 when certain general and permanent laws related to vessels and seamen were enacted as subtitle II of the title 46, United States Code.

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CHAPTER 313 -- COMMERCIAL INSTRUMENTS AND MARITIME LIENS

Codification of the Ship Mortgage Act, 1920
(46 App. U.S.C. 911-984)

SUBCHAPTER I -- GENERAL

Section 31301 -- Definitions

Section 31301(1) defines "documented vessel" as one documented under the laws of the United States as provided for under chapter 121 of title 46, Documentation of Vessels. This replaces 46 App. U.S.C. 911(1)(2) and (4) and repeals without replacement section 911(3)

Section 31301(2) defines "mortgagee" as the trustee designated in a deed or a bond issued under a deed. This is similar to the existing definition in 46 App. U.S.C. 911(5).

Section 31301(3) defines "necessaries" to include repairs, supplies, towage, and the use of a drydock and marine railway for a vessel. As in all codifications, the term "includes" means "including but is not limited to". The definition is new, is based on 46 App. U.S.C. 971-974, and makes no substantive change to law.

Section 31301(4) defines "preferred maritime lien" to mean a lien on a vessel that arises before a preferred mortgage is recorded and endorsed under sections 31321 and 31322 of this title for damages arising out of maritime tort, stevedore wages, crew wages, general average, and salvage. The definition is new, is based on 46 App. U.S.C. 953(a), and makes no substantive change to law.

Section 31301(5)(A) defines "preferred mortgage" to mean a mortgage that meets the requirements of section 31322. (See 46 App. U.S.C. 922(b))

Section 31301(5)(B) defines "preferred mortgage" to also mean a mortgage on a documented foreign vessel that is preferred under sections 31325 and 31326 for purposes of enforcement of the outstanding mortgage indebtedness. It also excepts foreign vessels of less than 200 gross tons. Preference is only granted if the mortgage was executed under the laws of a foreign country, registered under those laws in a public register at the port of registry or at a central office. (See 46 App. U.S.C. 951, second paragraph, less the Proviso.)

Section 31301(6) defines "Secretary" to mean the head of the department in which the Coast Guard is operating. This is new and is included to assure that the functions related to recordation of mortgages remains with the Coast Guard.

Section 31302 -- Availability of Instruments, Prescribing Fees, and Acknowledgment Requirement

Section 31302 provides for the public inspection of recorded instruments and for reasonable fees for copies. It also requires that an instrument to be recorded must be acknowledged before a notary or other proper official. (See 46 App. U.S.C. 926(b) and 927)

Section 31303 -- Certain Civil Actions Not Authorized

Section 31303 makes it clear that, if a mortgage covers a vessel and additional property that is not a vessel, this chapter does not authorize a civil action in rem in admiralty to enforce rights against the additional property. (See 46 App. U.S.C. 954(b))

Section 31304 -- Liability for Noncompliance

Section 31304 imposes liability on the United States Government for losses caused because the Secretary did not comply with statutory requirements. It imposes liability on the mortgagor if the mortgagor, master, or other individual in charge of the vessel does not comply with the statutory requirements. A civil action may be brought in a district court of the United States for losses incurred. If the plaintiff prevails, the court shall award costs and an attorney's fee to the plaintiff. (See 46 App. U.S.C. 941(c))

Section 31305 -- Waiver of Lien Rights

Section 31305 provides for the waiver of lien rights by the mortgagee or a person performing or supplying necessaries. (See 46 App. U.S.C. 974)

Section 31306 -- Rules of Law Not Affected

Section 31306 provides for the retention of certain rules in existence on the date of enactment of the Ship Mortgage Act, 1920 on June 5, 1920, concerning certain rights, laches, rankings, and priorities. (See 46 App. U.S.C. 974)

Section 31307 -- Regulations

Section 31307 authorizes the Secretary to prescribe regulations that the Secretary considers necessary. (See 46 App. U.S.C. 983)

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SUBCHAPTER II -- COMMERCIAL INSTRUMENTS

Section 31321 -- Recording and Discharge

Section 31321 provides for the recordation and discharge of a bill of sale, conveyance, mortgage, or assignment of a mortgage that includes any part of a documented vessel. When recorded with the Secretary, it is valid to the extent the vessel is involved, against any person except the grantor, mortgagor, or assignor, their heirs or devisees, and a person having actual notice of that instrument. (See 46 App. U.S.C. 921(a))

To be recordable, these instruments must: (1) state the interest of the grantor, mortgagor, or assignor; (2) state the interest sold, conveyed, mortgaged or assigned; and (3) be acknowledged as provided in section 31302(d). (See 46 App. U.S.C. 926)

This section requires the Secretary to record these instruments in the order they are received for recordation, and to maintain certain indexes. These indexes shall include the names of the vessels; names of the parties to the instruments; time and date each instrument was received; the interest in the vessel that was sold, conveyed, mortgaged, or assigned; and the date of the maturity of the mortgage. (See 46 App. U.S.C. 921(b))

Upon discharging any part of the indebtedness under a mortgage that is recorded, the mortgagor shall provide the Secretary with a written, acknowledged certificate of discharge of the indebtedness. The Secretary shall then record the certificate. If the vessel is covered by a preferred mortgage, the Secretary shall also endorse the discharge on the vessel's certificate of documentation. This endorsement will provide the vessel with the necessary documentation to clear with the U.S. Customs Service for a foreign voyage. (See 46 App. U.S.C. 925(b))

Section 31322 -- Preferred Mortgages

Section 31322 sets out the conditions that must be met for a mortgage to be considered a preferred mortgage, and the types of endorsements that the Secretary must make on any certificate of documentation of a vessel that is to be covered by a preferred mortgage.

Subsection (a) states that a preferred mortgage is a mortgage that includes the whole of a documented vessel (with some limited types of vessels excepted); is recorded under section 31321; provides for mortgage separability of vessel and additional property that is not a vessel; is properly endorsed by the Secretary; is accompanied by an affidavit that the mortgage has been made in good faith and without any design to hinder or defraud creditors or lienors; does not include a waiver of preferred status; and has as a mortgagee those enumerated in subsection (b)(7). (See 46 App. U.S.C. 922(a))

Subsection (b) applies to a mortgage that covers a vessel and additional property that is not a vessel. In this case, the mortgage may be a preferred mortgage only if the mortgage provides for the separate discharge of the additional property by paying a specified part of the mortgage indebtedness. In other words, there must be a means of separating the two or more mortgaged interests. (See 46 App. U.S.C. 922(e))

Subsection (c) permits a preferred mortgage to have any rate of interest that is agreeable to the parties to the mortgage. (See 46 App. U.S.C. 926(d))

Subsection (d) requires the Secretary, in all cases involving preferred mortgages, to endorse the certificate of documentation of a vessel indicating names of mortgagor and mortgagee; time and date of endorsement; amount of mortgage; date of maturity; separability of mortgage amount for vessel; and, if mortgage covers more than one vessel, the specified amount applicable to that vessel. (See 46 App. U.S.C. 922(c) and (b))

Subsection (e) applies when a preferred mortgage covers more than one vessel, does not provide for the separate discharge of a vessel, and is to be sold by court order. The amount of the mortgage indebtedness attributable to a vessel is that part of the indebtedness, increased by 20 percent, that the court determines approximates the value that the particular vessel bears to the value of all the vessels covered by the mortgage. In other words, the amount to be set by the court is the estimated value of the one vessel plus 20 percent of that value to assume sufficiency. (46 U.S.C. 922(f))

Subsection (f) permits clearing the vessel for a foreign voyage only after the endorsements required by subsection (d) have been made. (See 46 App. U.S.C. 922(d))

Section 31323 -- Disclosing and Incurring Obligations Before Executing Preferred Mortgages

Section 31323 provides for disclosure of obligations before executing a preferred mortgage and the incurring of obligations, after executing a preferred mortgage and before recordation. The mortgagor may not incur, without consent of the mortgagee, any contractual obligation establishing a lien on the vessel -- except a lien for stevedore wages, crew wages, general average, and salvage. Should a mortgagor be convicted of a violation of this section then the mortgage indebtedness, at the option of the mortgagee, is payable immediately. (See 46 App. U.S.C. 924 and 941(b))

Section 31324 -- Retention and Examination of Mortgages and Documents of Self-Propelled Vessels Covered by Preferred Mortgages

Section 31324 provides for the retention and examination of mortgages and documents of a self-propelled vessel that is covered by a preferred mortgage. A certified copy of the mortgage shall be on board and made available to persons that have business with the vessel that may give rise to a maritime lien or the sale, conveyance, mortgage, or assignment of the mortgage. (See 46 App. U.S.C. 923)

Section 31325 -- Preferred Mortgage Liens and Enforcement

Section 31325 provides for the enforcement of a preferred mortgage lien. A "preferred mortgage" is a lien on the vessel in the amount of the outstanding mortgage indebtedness secured by the vessel. On default of any term, the mortgagee may enforce the preferred mortgage lien in a civil action in rem in admiralty, or in personam in admiralty against the mortgagor for the amount of mortgage indebtedness secured by the vessel or any deficiency in paying off that indebtedness. Subsection (c) provides for original jurisdiction by a district court of the United States, to the exclusion of the courts of a State.

Subsection (d)(1) provides that actual notice of a civil action in rem in admiralty must be given in a manner directed by the court to the master, individual in charge of the vessel, and any person that recorded a notice of a claim of an undischarged lien. This notice is not required if, after a search is made that is satisfactory to the court, the person entitled to notice is not found in the United States. Failure to give notice does not affect the court's jurisdiction. However, the mortgagor is still liable to the person not notified for damages in the amount of that person's interest in the vessel that was terminated by the civil action in rem, and a civil action may still be brought to recover the amount of the terminated interest. The district courts have original jurisdiction of the action, regardless of the amount in controversy or the citizenship of the parties. If plaintiff prevails, the court shall award costs and attorney fees to the plaintiff.

Subsection (e) provides that, in a civil action in rem, the court may appoint a receiver and authorize operation of the vessel. When directed by the court, a United States marshall may take possession -- even if the vessel is in the possession of or under the control of a person claiming a possessory common law lien. (See 46 App. U.S.C. 951, 952, and 954(a))

Section 31326 -- Court Sales to Enforce Preferred Mortgage Liens and Priority of Claims

Section 31326 provides for a court-ordered sale to enforce a preferred mortgage lien and the priority of claims. When a mortgaged vessel is sold by court order in a civil action in rem, any prior claim in the vessel is terminated -- including any possessory common law lien. Each of these terminated claims attaches, in the same amount and priority, to the proceeds of sale -- except that the preferred mortgage lien always has priority over these other claims. However, the preferred mortgage lien is still subordinated to expenses and fees allowed by the court, costs imposed by the court, and any preferred maritime liens. In the case of a foreign vessel, the preferred mortgage lien is also subordinated to a maritime lien for necessaries performed or supplied for the vessel in the United States. (See 46 App. U.S.C. 953(b), and the second paragraph Proviso of 951)

Section 31327 -- Surrender of Documents of Preferred Mortgage Vessels

Section 31327 provides for surrender of the certificate of documentation of a vessel covered by a preferred mortgage if the mortgagee consents and the Secretary approves -- except when a vessel is forfeited or sold by order of a United States or foreign court. (See 46 App. 961(a))

Section 31328 -- Forfeiture of Mortgagee Interest

Section 31328 provides for forfeiture of the mortgagee's interest if the mortgagee authorized, consented, or conspired to do the act, failure, or omission that is the basis of the violation that caused forfeiture of the vessel. (See 46 App. U.S.C. 961(b))

Section 31329 -- Limitations on Providing Mortgaged Vessel Interests to Persons Not Citizens

Section 31329 imposes limitations on providing mortgaged vessel interests to persons not citizens of the United States. It requires the Secretary to approve the trustee, if the trustee is a bank or a trust company -- and sets a number of qualifications the trustee must meet, one of which is United States citizenship.

If the trustee fails to meet these qualifications at any time, the Secretary must disapprove the trustee. The Secretary may approve the assignment of a right under the mortgage to a person not a citizen of the United States. In a civil action in rem, the vessel may be sold, by court order, to a person not a citizen of the United States only with the approval of the Secretary. Any issuance, transfer, or assignment of an evidence of indebtedness made contrary to these provisions is void. (See 46 App. U.S.C. 961(d), (e), and (f))

Section 31330 -- Penalty

Section 31330 provides for criminal penalties for failure to disclose obligations that are required or for incurring contractual obligations establishing liens on a vessel after executing a preferred mortgage and prior to recording. It also makes the president or chief executive officer of a corporation or association liable as a mortgagor for the penalties under this section. (See 46 App. U.S.C. 941(b))

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SUBCHAPTER III -- MARITIME LIENS

Section 31341 -- Persons Presumed to Have Authority to Procure Necessaries

Section 31341 lists those persons who are presumed to have authority to procure necessaries for a vessel. These include the owner, master, or a manager at the port of supply; and an officer or agent appointed by the owner, charterer, owner pro hac vice, or buyer in possession of the vessel. Any person who is not properly in possession of or in charge of a vessel has no authority to procure necessaries. (See 46 App. U.S.C. 972, 973)

Section 31342 -- Establishing Maritime Liens and Enforcement

Section 31342 provides that any authorized person providing necessaries for a vessel has a maritime lien on the vessel, may bring a civil action in rem in admiralty to enforce the lien, and is not required to allege or prove that credit was given to the vessel. (See 46 App. U.S.C. 971, 974)

Section 31343 -- Court Sales to Enforce Maritime Liens

Section 31343 provides that any person claiming a lien on a vessel covered by a preferred mortgage may record a notice of lien. This notice must state the nature of the lien, date it was established, the amount, the name and address of the person claiming a lien, and it must be acknowledged. The Secretary must record a notice of lien if it complies with these requirements. When any part of the indebtedness is discharged, the claimant shall provide the Secretary with a written, acknowledged certificate of discharge of the indebtedness and the Secretary shall record the certificate. (See 46 App. U.S.C. 925(a) and (26(b))

Section 31344 -- Court Sales to Enforce Maritime Liens

Section 31344 provides for the sale of a vessel to enforce a maritime lien -- free of all prior claims -- other than a preferred maritime lien. However, on request of the mortgagee (original borrower), plaintiff, or intervenor, the court shall require the buyer to give and the mortgagee to accept a new mortgage on the vessel for the time remaining under the original mortgage. The new conditions should be the same as those of the original mortgage and must be court approved. When a new mortgage is given, the mortgagee may not be paid from the proceeds of sale but the amount payable shall be reduced by the amount of the new mortgage indebtedness. (See 46 App. U.S.C. 961(a))

Section 31345 -- State Statutes Superseded

Section 31345 provides for preemption of State laws to the extent a claim for necessaries is enforced by a civil action in rem in admiralty against the vessel. (See 46 App. U.S.C. 975)

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CHAPTER 315 -- PUBLIC VESSELS AND GOODS

This part of H.R. 3105, which merges the Suits in Admiralty Act (46 App. U.S.C. 741-752) and the Public Vessels Act (46 App. U.S.C. 781 et seq.), will not be considered at this time.

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Section 2 -- Legislative Purpose and Construction

Section 2 of H.R. 3105 contains miscellaneous provisions related to the purpose and construction of this legislation. They are standard provisions protecting existing law. The subsections refer to laws repealed by this legislation; any pending court cases; current regulations, rules or orders; and severability.

Section 3 -- Repeals

Section 3 of H.R. 3105 contains miscellaneous provisions related to the repeal of existing laws that are codified and reenacted by the bill. It repeals other statutes that are executed, superseded, obsolete, or otherwise of no legal effect. It also preserves the rights and duties that matured, penalties that were incurred, and proceedings that were begun before the date of enactment of this legislation. The repeal of the original Act also repeals all amendments to that Act. (This section will have to be amended to exclude any references to the Suits in Admiralty Act, 46 App. 741-752.)

STATEMENT OF RICHARD B. BARNETT
Chairman, Committee on Marine Finance
The Maritime Law Association of the United States
Before
House Subcommittee on Merchant Marine
on June 28, 1988
Concerning H.R. 3105

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

I thank you for the opportunity to appear before this Committee. For many years, as a partner in the law firm of Haight, Gardner, Poor & Havens, I have specialized in ship financing. Today, I am here in my capacity as Chairman of the Committee on Marine Finance of The Maritime Law Association of the United States.

The Maritime Law Association of the United States, or MLA as it is commonly referred to, was organized in 1899 in New York City. Today, the MLA has more than 3,200 members who come from all states and territories where there is maritime activity, the heaviest concentrations being in New York, Louisiana, California and Texas.

The purposes of the MLA, as expressed in its Articles of Association, are "to advance reforms in the maritime law in the United States, to facilitate justice and its administration, to furnish a forum for the discussion and consideration of problems affecting the maritime law and its administration and to act with foreign and other associations in efforts to bring about a greater harmony in the shipping laws, regulations and practices of different nations."

The Committee on Marine Finance of The Maritime Law Association of the United States consists of more than 80 lawyers whose practice includes a substantial amount of ship financing and who have a great interest in the recodification of the Ship Mortgage Act and proposed changes therein.

Prior to the passage of the Ship Mortgage Act in 1920, little financing was available to shipowners based upon the asset value of the ship itself. The reason was that a mortgage on a ship was considered a non-maritime claim, which ranked behind all maritime liens. In the United States most trade debt claims, including claims for supplies to the ship and repairs, have maritime lien status.

To encourage investment in shipping, Congress passed the Ship Mortgage Act which gives maritime lien status to mortgages on ships and a priority over most trade debt claims if various formalities are complied with.

Over the years, the Ship Mortgage Act has in general served its purpose well, giving lenders a security interest in the ship which is recognized not only by the courts in the United States but courts throughout the world where foreclosure proceedings take place. The Ship Mortgage Act has also been the model for similar legislation in other countries such as Liberia, the Philippines and Vanuatu. However, the Ship Mortgage Act needs minor modifications to accomplish three purposes:

(1) to enable the Ship Mortgage Act to accommodate modern financing techniques;

(2) to eliminate certain of the formal requirements in the Act that experience has demonstrated are unnecessary or obsolete; and

(3) to clarify certain of the provisions of the Act where required as a result of court decisions and agency rulings since the Ship Mortgage Act was adopted.

The proposed recodification of the Ship Mortgage Act included in H.R. 3105 presents an opportunity to accomplish these purposes. The Committee on Marine Finance of The Maritime Law Association has developed the following recommendations which have been endorsed by the MLA Executive Committee:

First, we recommend that certain of the formal requirements, which must be met for a valid mortgage to be awarded preferred status under the Act, be eliminated. These requirements are as follows:

(a) the requirement that the mortgage particulars be endorsed on the ship's Certificate of Documentation;

(b) the requirement that an affidavit be filed with the mortgage, when recorded, to the effect that the mortgage is made in good faith and without any design to hinder, delay or defraud creditors;

(c) the requirement that a mortgage not stipulate that the mortgagee waives the preferred status thereof.

All these requirements are retained in the proposed recodification.

Our view is that the endorsement provision no longer serves a useful purpose. While suppliers in foreign ports may in 1920 have asked to see the ship's Certificate of Documentation to determine whether it was safe to extend credit to the ship, because of present day communication techniques this is no longer the case. In fact, the amount of the mortgage shown on the Certificate of Documentation frequently bears little relevance to the actual amount of indebtedness outstanding. Furthermore, the need to endorse in order to perfect a mortgage unduly complicates the financing transaction since the perfection of the mortgage lien on a particular ship can be accomplished only when that ship is in port and its Certificate of Documentation is available for endorsement by a Coast Guard officer. If a shipowner is financing a fleet of ships, the endorsement requirement may give rise to the need for a series of time consuming and expensive, separate takedowns of its loan since all ships in the fleet are unlikely to be in port at one time.

The Affidavit of Good Faith has become a meaningless, time-consuming formality.

The requirement that a mortgage not stipulate that the mortgagee waives the preferred status thereof is a puzzling provision and should be eliminated. As at least one commentator has stated -- why would a mortgagee go through all the formalities to create a preferred mortgage and then waive the preferred mortgage status. The only real effect of the provision is to cause lawyers concern in making sure that particular mortgage provisions do not constitute an inadvertent waiver of preferred status.

Second, we recommend that the provisions dealing with the amount of the mortgage be clarified.

At the time the Ship Mortgage Act was adopted, a financing was typically a simple transaction involving a loan payable in installments over a period of years with interest at a fixed rate. Today a variety of financing options are provided by lenders, including revolving credit loans, letters of credit and multi-currency options. These financing arrangements do not always fit comfortably within the framework of the Ship Mortgage Act.

The Ship Mortgage Act requires that the amount of the mortgage be endorsed upon the Certificate of Documentation and that the amount of the mortgage be shown in the books kept by the Coast Guard Documentation Officers for the recording of mortgages. Even if the endorsement provision in the Act is eliminated as we recommend, the provision for recording the amount of the mortgage should be retained. The Brussels Convention of 1967 dealing with maritime liens and mortgage provides for recognition by states which are contracting parties to the Convention of foreign mortgages only if, among other things, "the amount secured" is included as part of the recording information. Even though the Brussels Convention has not been ratified by a sufficient number of countries to bring it into effect, its provisions have been adopted as domestic law by certain countries, including the Scandinavian countries. To insure recognition of United States ship mortgages in such countries, the requirement for recording the amount of the mortgage should be retained.

However, questions frequently arise as to what the proper amount is for recording and endorsement purposes in transactions such as revolving credit loans where the amount outstanding may vary from time to time. The statutory language should be clarified so that there is no question that the proper amount for recording purposes is the maximum principal amount, which may be outstanding at any one time. The question of mortgages in foreign currencies or with multi-currency options should also be addressed. The Liberian law, which is based on the Ship Mortgage Act, has already been amended to eliminate the endorsement provisions and to clarify the amount requirement for recording purposes.

Third, the ability of a WESTHAMPTON trustee to purchase a United States flag ship at foreclosure sales should be clarified. The Ship Mortgage Act requires that the mortgagee be a citizen of the United States within the meaning of Section 2 of the Shipping Act and further provides that upon foreclosure of a mortgage, no ship of the United States may be sold to any person not a citizen of the United States within the meaning of Section 2 of the Shipping Act. Foreign lenders are encouraged to participate in the financing of United States flag vessels through the mechanism set forth in Public Law 89-346 adopted in 1954. Under these provisions, the foreign lenders designate a United States citizen corporate trustee to hold the mortgage on behalf of the foreign lenders. The United States Maritime Administration has taken the position that such a trustee, commonly referred to as a WESTHAMPTON trustee, can institute foreclosure proceedings to enforce the mortgage in the United States but cannot buy-in the ship at the foreclosure sale. This puts the foreign lenders at a marked disadvantage compared to United States lenders. If market conditions are bad, as they usually are when a mortgage is foreclosed, the only way a lender can hope to recover its investment is to buy-in the ship at the foreclosure sale and hold it until market conditions improve at which time the ship will be resold. The Maritime Administration's position precludes the use of this procedure by foreign lenders. The law should be clarified to permit the trustee acting for foreign lenders to buy-in at the foreclosure sale. Ships so purchased could not be transferred to foreign registry or sold to a non-citizen without Maritime Administration approval.

We support the language which we understand was prepared for this purpose by members of the Staff. We suggest consideration of one additional paragraph to make it clear that no change is contemplated in existing law in the case where the trustee and all the lenders are citizens of the United States.

Fourth, the jurisdiction of certain territorial courts should be clarified. The Ship Mortgage Act provides that original jurisdiction of all suits to enforce ship mortgages is granted to the District Courts of the United States exclusively. Questions have arisen concerning the jurisdiction of the High Court of American Samoa and certain other courts to enforce ship mortgages. To encourage investment in fishing vessels and other ships that regularly call at such ports, such courts should have jurisdiction to enforce ship mortgages. We recommend that the Act be clarified in this respect.

Fifth, mortgages and other instruments should be valid when filed for recording. The Ship Mortgage Act contemplates, and the practice for many years has been, that a ship mortgage or other conveyance, if in proper form, will be recorded substantially simultaneously with its presentation to the Coast Guard Office.

However, budgetary cutbacks involving the Coast Guard have taken place at a time when the volume of instruments presented for recording has substantially increased, partly as a result of the vast expansion of yacht financing which has taken place. The result is that a substantial time gap may now occur between the time the instrument is filed for recording and the time recording actually takes place. This period may run many months. A recent Third Circuit case* dealt with a situation where a shipowner went bankrupt between the time the mortgage was presented for recording and the time the actual recording took place. The trustee-in-bankruptcy argued that the mortgage had never been properly perfected before the bankruptcy occurred. The Court stretched the provisions of the Ship Mortgage Act to provide that the mortgage recording was effective from the time of filing provided that the files of the Coast Guard were available for public inspection so that a potential creditor could have learned of the existence of the mortgage from review of the Coast Guard records. The Federal Aviation Act dealing with the recording of mortgages on aircraft explicitly provides that the instrument shall be effective from filing. We propose that the Ship Mortgage Act be revised to include a similar provision so that a mortgage would be valid from the time of filing if the ship at such time is a documented ship or if an application for documentation has been made and all required fees paid.

We urge the adoption of the foregoing recommendations. We believe the effect will be to benefit the shipping industry by facilitating the financing of ships.

Suggested language for the changes we have recommended is included as an exhibit to my statement.

On behalf of The Maritime Law Association of the United States, thank you for the opportunity which you have given us to present these views.

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*In Re Alberto, 823 F.2d 712 (3rd Cir. 1987).

SUMMARY OF PROPOSALS OF THE MARITIME LAW ASSOCIATION

I. Abolish the following requirements:

1. Section 31322(a)(4), (d): Endorsement of mortgage on vessel's Certificate of Documentation;

2. Section 31322(a)(5): Affidavit of Good Faith;

3. Section 31322(a)(6): No stipulation of waiver of preferred status.

II. Add one of the following proposals to Section 31301 to define the "amount of mortgage":

1. "'Amount of the Mortgage' shall, for the purposes of Section 31321(c)(2)(E) and Section 31322(d)(4) [assuming endorsement on vessel's Certificate of Documentation] of this Chapter, mean the maximum amount of principal which is or may become secured by the mortgage for which the mortgagor is directly or contingently liable."

2. "'Amount of the Mortgage' shall, for the purposes of Section 31321(c)(2)(E) and Section 31322(d)(4) [assuming endorsement on vessel's Certificate of Documentation] of this Chapter, mean the maximum amount of principal which is or may become secured by the mortgage for which the mortgagor is directly or contingently liable stated at the time of recordation of the mortgage either in U.S. Dollars or in some other currency, with the equivalent number of U.S. Dollars set forth, calculated at the applicable exchange rate prevailing on the date of execution of the mortgage. If the mortgagee or mortgagor exercises any option or options reflected in the mortgage to change the currency in which the obligation secured or to be secured by the mortgage is payable, no change shall be required in the 'amount of the mortgage' as initially recorded."

3. The following are provisions from Liberian law:

SECTION 106A

Advances and Repayments. - (1) A Preferred Mortgage shall not be extinguished or lose its priority because all previously outstanding obligations secured thereby have been fully repaid or otherwise performed, provided that an advance or other value is to be given at a later time pursuant to commitment existing at the time the Mortgage is recorded. For the purpose of this paragraph an advance or other value is given "pursuant to commitment" if the mortgagee or other person entitled to the benefit of the security of the mortgage has bound himself to give it, whether or not a subsequent event of default or other event not within his control has relieved or may relieve him from his obligation.

(2) When a Preferred Mortgage secures an obligation in respect of which one or more advances or repayments may be made from time to time in the future and the maximum amount outstanding under the obligation at any one time is limited to a certain amount, the amount to be recorded with respect to such obligation may be either:

(a) such maximum amount that may be outstanding at any one time, or

(b) the aggregate of all possible advances that may be made.

The recording shall clearly indicate whether the amount is the maximum amount that may be outstanding at any one time or is the aggregate of all possible advances.

Eff. Dec. 24, 1984; amended eff. Aug. 28, 1986.

SECTION 106B

Units of Account. - (1) The obligations secured by a Preferred Mortgage may be expressed in any unit or units of account to which the parties may agree, including but not limited to currency of the Republic of Liberia, currency or currencies of any foreign state or states, or in equivalents of any other unit or units of account established by intergovernmental organizations.

(2) If a Preferred Mortgage secures an obligation in one or more specified units of account and there is an option to have a unit of account altered from time to time, the principal amount of the mortgage to be recorded shall be denominated in one or more of the said specified units of account. The recordation may include as additional words "or an equivalent amount in any alternate unit of account," or similar language, and if such additional words are recorded, no change in the recorded amount shall be required to reflect the fact that the obligation or any portion thereof is subsequently denominated in a different unit or units of account, unless the parties otherwise agree.

(3) When a Preferred Mortgage secures an obligation in respect of which there is an option to have the obligation amount denominated from time to time in alternate units of account but which continues to be payable in, or by reference to, a specified unit of account:

(a) the amount of the obligation to be recorded shall be expressed in the specified unit of account; and

(b) notwithstanding any exercise of the option, no change in the recorded amount shall be required.

(4) A Preferred Mortgage as described in paragraphs (2) or (3) of this Section 106B may additionally secure any loss up to a specified amount arising out of fluctuations between a specified unit of account and any alternate unit of account in which the obligation amount may be denominated from time to time, and such specified amount shall also be recorded.

Eff. Dec. 24, 1984; amended eff. Aug. 28, 1986.

III. Abolish Section 31321(d)(1): Requirement to file with secretary a partial discharge of mortgage indebtedness.

IV. Add the following language to the Committee proposal concerning the WESTHAMPTON TRUSTEE:

"(f)(1) A documented vessel may be sold by order of a district court of the United States in a civil action in rem in admiralty only to --

"(i) a citizen of the United States; or

"(ii) citizen of the United States that is a trustee approved by the Secretary of Transportation under paragraph (e) of this subsection acting on behalf of holders of indebtedness secured by a preferred mortgage in favor of that trustee, even if some or all of the holders are not citizens of the United States.

"(2) When a vessel is sold to a trustee under clause (1)(ii) of this paragraph --

"(i) the trustee may not, without the approval of the Secretary, sell, mortgage, lease, charter, deliver, or in any manner transfer, or agree to sell, mortgage, lease, charter, deliver, or in any manner transfer, to any person not a citizen of the United States, or transfer or place under foreign registry, the vessel or any interest in the vessel;

"(ii) the trustee may not operate the vessel without the approval of the Secretary;

"(iii) the vessel, when owned by the trustee, is subject to section 902 of the Merchant Marine Act, 1936 (46 App. U.S.C. 1242); and

"(iv) the sale of the vessel to the trustee is not considered a sale foreign within the terms of the first proviso of section 27 of the Merchant Marine Act, 1920 (46 App. U.S.C. 883).".

"(g) Nothing contained in subsection (f) shall be deemed to limit the right of a trustee acting on behalf of holders of an indebtedness all of whom are 'citizens of the United States'."

V. Add to Section 31325(c):

1. "For purposes of this subsection 'district court of the United States' shall include the District Courts of Guam, Northern Mariana Islands and the Virgin Islands as well as the High Court of American Samoa."

VI. Add the following language to Section 31321:

1. "Each conveyance, mortgage or other instrument recorded by means of or under the system provided for in subsection (a), (b) or (c) of this section shall from the time of its filing for recordation be valid as to all persons without further or other recordation if the vessel is duly documented or, alternatively, if application for such documentation and all required supporting instruments have been duly filed with appropriate fee(s) as provided in the Vessel Documentation Act of 1980, as amended, or in any statute which may replace such act. If any required instruments have not been filed or fees have not been paid, the effective date of the conveyance mortgage, or other instrument will be postponed until the date as of which all of such instruments and fee(s) shall have been duly filed."

VII. Amend Section 31302(a):

"(a) An instrument filed for recording or recorded with the Secretary under this Chapter is available for public inspection."

VIII. Amend Section 31321(a):

"(a) A bill of sale, conveyance, mortgage, or assignment of a mortgage that includes any part of a documented vessel must be filed for recordation with the Secretary to be valid, to the extent the vessel is involved . . . ."

PREPARED STATEMENT OF GREGORY PROTEAU, EXECUTIVE DIRECTOR, NATIONAL MARINE BANKERS ASSOCIATION -- PRESENTED BY C. PETER THEUT, GENERAL COUNSEL, NMBA, BEFORE THE SUBCOMMITTEE ON MERCHANT MARINE, 28 JUNE 1988

On behalf of the 144 members of the National Marine Bankers Association, who hold recreational boat loan portfolios of approximately $4 billion, I wish to convey two primary concerns about efforts to revise, consolidate, and enact certain laws related to maritime commercial instruments and liens.

Our first concern is that lien perfection afforded by the Ship Mortgage Act of 1920 is an excellent way to secure loans made on so-called documentable vessels. Though ponderous and perhaps archaic, gaining a first preferred ship's mortgage on large boat transactions is a routine practiced by the majority of our members. We are amenable to changes proposed which would simplify and/or clarify the lien procedure, however, we would oppose any revisions which would lessen the power of the ship's mortgage or dilute our security interests. NMBA continues to discuss this issue with members of the maritime law community and defers to its expertise in determining which changes would be beneficial or detrimental. We would also encourage the committee to continue its dialogue with admiralty attorneys along these lines.

A second, much broader area also merits commentary. While NMBA members -- and the documentable boat-owning populace -- enjoy the protection afforded by the first preferred ship's mortgage, America's small boat lenders and owners share no similar, uniform method of lien perfection. Consider for a moment that in the U.S. for every registered pleasure boat above 26-feet, there are forty (40) registered boats below that length. Although you can place a ship's mortgage on those recreational vessels of 28- to 30-feet in length, how do lenders secure loans on smaller craft? How do owners buy or obtain loans on smaller craft knowing they are clear of other outstanding liens?

Boat title laws on -- or soon to be on -- the books in 24 states provide a "second best" form of lien perfection for lenders and owners. The problem is that these laws are anything but uniform, often don't cover the same products or offer reciprocity. In states without title laws, small boat liens are perfected via the Uniform Commercial Code, a literal quagmire of differing jurisdictional options. In either of these situations, with titling or UCC filings, the protections against theft or fraudulent transfer of individuals' boats is great. Likewise, for lenders, the opportunity for the loan on the small boat to default greatly increases. As you might expect, lenders have less desire to make small boat loans because of the current problems with boat title or UCC filings.

Since its founding nine years ago, our organization has been supportive of efforts to standardize lien procedures for all recreational vessels with emphasis in the small boat arena. We feel positive about the general provisions of H.R. 3298 introduced last year by Congressman Robert Davis.

It appears to us, that certain provisions of H.R. 3298 -- to gain nationally-uniform boat titling laws for undocumented vessels with centralized recordation of security interests -- would be natural complements to this Committee's work on H.R. 3105 since both encompass consideration of maritime instruments and liens. We would be delighted to work with you in achieving these goals which would benefit America's boat owners and the marine financial community.

Thank you for the invitation to present our ideas and concerns.

PREPARED STATEMENT OF BRUCE A. KING, BOGLE & GATES, ON BEHALF OF THE SECTION OF BUSINESS LAW OF THE AMERICAN BAR ASSOCIATION, BEFORE THE SUBCOMMITTEE ON MERCHANT MARINE, 28 JUNE 1988

It is an honor to appear before this subcommittee to testify on the proposed recodification of the Ship Mortgage Act, 1920.

I am a partner in the Seattle, Washington law firm of Bogle & Gates, where I specialize in maritime finance and regulation. Also, I am the vice-chairman of the Subcommittee on Maritime Financing of the American Bar Association (the "ABA"). This is a subcommittee of the Commercial Financial Services Committee of the ABA's Section on Business Law. For the past three years the ABA subcommittee has been at work on a proposal for substantive revisions to the Ship Mortgage Act. It has gone through several drafts, and its current draft, dated April 2, 1988 and which was furnished to your staff as requested, is in the format of proposed changes to H.R. 3105. Unfortunately, there was not time before this hearing took place for me to take all of the steps necessary to obtain official approval to speak on behalf of the ABA or its Section on Business Law. Consequently, at this point I must express my views on the Ship Mortgage Act and interpret the work product of the ABA subcommittee in my capacity as a private citizen. When the necessary official approval from the ABA is obtained for my remarks, I will inform this subcommittee so that this fact can be made a part of the record. *

The recodification of the Ship Mortgage Act presents an ideal opportunity to not only rephrase it in a modern format consistent with the ongoing recodification of Title 46 of the United States Code, but also to eliminate antique provisions that serve no useful purpose in modern vessel financing, many of which amount to little more than traps for unwary lenders and counsel. It also presents an opportunity to simplify the procedures for using the ship mortgage as a financing device, thus making financing a vessel less cumbersome and expensive. These costs are almost invariably passed onto the borrower, who, for the most part, are small businessmen and yacht owners.

Just as the ABA subcommittee was beginning its work in drafting proposed substantive revisions to the Act, the ongoing recodification of Title 46 reached the Ship Mortgage Act, producing H.R. 3158, the predecessor to H.R. 3105. When H.R. 3158 was introduced, a special subcommittee of the Maritime Law Association of the United States (the "MLA") was formed to review H.R. 3158 with the view toward identifying and suggesting any necessary corrections to insure that the bill did not inadvertently change existing law in the course of recodifying it. The ABA subcommittee kept in contact with the MLA subcommittee, and the ABA subcommittee's current draft adopted the vast majority of the MLA subcommittee's suggestions. Thus, the ABA subcommittee's current draft incorporates four elements: (1) the proposed recodification, now H.R. 3105, (2) the ABA subcommittee's suggestions for substantive changes to existing law, (3) most of the MLA subcommittee's suggestions for technical corrections to H.R. 3105, to the extent they are applicable to the remaining provisions of H.R. 3105, and (4) a few technical corrections suggested by the ABA subcommittee. I should note for the record that the ABA subcommittee's work is yet in the draft stage, although an advanced stage.

While the ABA subcommittee has developed many changes, its central aim was to do so without seriously affecting the basic priority decisions embodied in the Ship Mortgage Act (and the hard-fought political compromises it represents). Before discussing in detail the principal substantive revisions and corrections included in the draft, I should like to address in general the necessity for reforms.

First, the Ship Mortgage Act has very technical provisions which enhance the cost of vessel financing for financial institutions and borrowers, and which cost the government a great

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*See September 15, 1988 letter from David E. Nelson, Chairman, Section of Business Law, American Bar Association deal in needless time spent by United States Coast Guard documentation officers. A security interest in a piece of land-based equipment -- that may cost several times what a fishing vessel may cost, for example -- can be granted and perfected for a fraction of the cost of granting and perfecting a security interest in a vessel, especially if the borrower is simultaneously acquiring the vessel. In other areas of financing, a borrower may sign and file security documents before he even acquires the collateral: in the course of the financing transaction, at the moment title to the collateral actually passes to the borrower, the security interest attaches. In ship financing, however, a preferred mortgage must not be executed prior to the date of the bill of sale conveying the vessel to the borrower, and the mortgage must be held in escrow until the Borrower has documented the vessel, unless a simultaneous, same-day closing and registration can be arranged. In multiparty transactions involving the repayment of prior financings, or the like, the logistics of orchestrating the movement of paper in closing a transaction can account for a major portion of the transactions costs involved.

Second, the Ship Mortgage Act contains antiquated and inexplicable provisions which can be a nuisance to comply with and which are traps for the unwary. For example, the law currently requires that a ship mortgage be accompanied by an affidavit to the effect that the shipowner granting the mortgage is doing so in good faith, without an intention of defrauding his creditors. It is difficult to imagine why a shipowner who would be willing to defraud his creditors by signing a mortgage would be unwilling to do so if he would also have to sign an affidavit concealing his improper intentions. While the requirement of such an affidavit was common in other areas of financing at the time the Ship Mortgage Act was enacted, it is easy to see why the affidavit of good faith has almost completely disappeared in modern financing. Unfortunately, however, while the requirement remains the affidavit of good faith cannot be casually treated as an idle formality. There has been a surprising amount of litigation over the years over alleged technical defects in the execution of affidavits of good faith. This culminated in 1986 in the case of Bank of Astoria v. M/V PACIFIC CONQUEST, 1986 A.M.C. 2182 (D. Or. 1986), in which a district court held that a mortgage of a yacht owned jointly by husband and wife forfeited its preferred status because of a defect in the execution of the affidavit. Because the husband was not available at the time the mortgage was signed, the wife signed the mortgage and the affidavit on behalf of herself and on behalf of her husband, who had granted her his general power of attorney. While the execution of a mortgage under a power of attorney was proper, the court ruled that an affidavit cannot be signed by a power of attorney.

As another example, the Ship Mortgage Act now contains a provision, 46 U.S.C. § 922(a)(4), which states that a preferred mortgage may not "stipulate that the mortgagee waives the preferred status thereof." As has been pointed out in a leading treatise on admiralty law, Gilmore & Black, The Law of Admiralty, 2nd Ed. 1979, p. 711, no one drafting a mortgage would consciously do this. The question remains, then, what the drafters of the Ship Mortgage Act intended by this provision. It has been construed to mean that the use of subordination agreements in vessel financing is impermissible, which greatly inconveniences modern financing, and it has also been interpreted by some as a suggestion that the technical requirements of the Ship Mortgage Act must be strictly construed, which is contrary to the general legal principle that substantial compliance with technical provisions of law is sufficient.

Partly due to the complicated nature of compliance with the Ship Mortgage Act, and also due to budgetary constraints, the Coast Guard has struggled for several years with serious backlogs in processing ship financing documents. This problem has been especially acute in the area of yacht financing. Not surprisingly, most Coast Guard offices give precedence to the processing of documentation for commercial vessels. With the delays in processing yacht documentation frequently in the three to six-month range, a serious problem has arisen for the yacht financing industry. The long delays mean that at any given time, a sizable portion of a lender's portfolio of loans is unsecured. Also, unless a yacht owner simultaneously registers the yacht with a state, the yacht owner is deprived of the benefits of documentation of the yacht, which may be essential if the yacht owner contemplates a foreign cruise.

There are several possible approaches toward dealing with the problem of the backlog in yacht transactions. One would be to greatly increase the appropriation to the Coast Guard so that it can have the manpower to handle all transactions in a timely manner. The Coast Guard has made great strides in making its own operations more efficient, but clearly there is a limit to what it is possible for it to do with limited resources. A second approach is to greatly simplify the steps necessary to perfect a mortgage with the Coast Guard. A third approach is to transfer the documentation of title and security interests in yachts to the states, conferring upon security interests perfected in the states the equivalent of preferred mortgage status, along the lines proposed by Congressman Davis last year. All of these approaches have desirable features, and it should be noted that the three approaches are not mutually inconsistent. The decision is largely one of budgetary and governmental policy, although there are a few issues which merit consideration in weighing the alternatives.

First, under current law, yachts can be registered in the various states or documented with the Coast Guard. They can even be registered in a state and documented with the Coast Guard simultaneously. This presents an obvious opportunity for fraud, because the owner of a yacht could register it with a state, borrow funds and grant a state-law security interest in the yacht, and simultaneously document the yacht with the Coast Guard, borrow money from a second lender and grant a preferred mortgage in the yacht to secure the second loan. Whatever solution is adopted to the question of yacht financing, this is an area that merits attention.

Second, if the registration of yachts and the perfection of security interests in yachts is completely delegated to the states, it may be necessary to make a provision for the issuance of a federal certificate of documentation for identification and nationality purposes. The document would not be used to perfect security interests, but would be used solely to enable a yacht owner to cruise conveniently in foreign waters. The owners of state-registered yachts who cruise to foreign countries occasionally have problems entering and clearing customs abroad because they lack federal documentation. A customs official in the Far East could be excused for not knowing what to make of a title certificate issued by, say, the State of Oregon, which may not even have the words "United States of America" on it.

Lastly, before all security interests in yachts are left to be perfected at the state level, it is important that it be verified that foreign courts will give recognition to the security as maritime liens.

The following summarizes some of the principal features of the ABA subcommittee's draft revisions to H.R. 3105. (Section references are to H.R. 3105 as modified by the ABA subcommittee's April 2, 1988 draft.)

1. As a convenience in closing financing transactions, at § 31322(a) mortgages "whenever made" are permitted, so that a preferred mortgage may be executed at any time in the closing of a transaction, even before the moment in time the grantor acquires title to the vessel.

2. As under current law, the entire mortgage instrument may be recorded, but, as an option, and a departure from current law, the ABA subcommittee draft provides, at § 31322(a)(2), that a simple notice of mortgage may be filed instead. In either event, the filed mortgage or notice of mortgage is sufficient if it contains five items of information: (a) the name of the owner; (b) the name of the mortgagee; (c) the mortgagee's address; (d) the name and official number of the vessel; and (e) the principal amount of the mortgage. Following the practice under the Uniform Commercial Code, the requirement that a mortgage or a notice of mortgage be acknowledged before a notary public has been deleted, and a notice of mortgage may be executed and recorded prior to the existence of the mortgage to which it pertains. This latter feature would enable the recording process to be taking place while the rest of the documents in the transaction are being prepared and executed. A sample of such a notice of mortgage is attached to this testimony.

3. Again, following the lead of the Uniform Commercial Code, the ABA subcommittee draft suggests at § 31322(b) that a mortgage granted in the context of a purchase of a vessel that is perfected after the passage of title to the vessel be deemed perfected as of the passage of title if the mortgage and the necessary documents are properly prepared and presented to the Coast Guard for processing within ten days after the passage of title to the new shipowner. This helps to deal with the inevitable gap in time between the moment when title passes and the time when all the documents can be processed.

4. Current law effectively precludes the use of so-called finance leases in the maritime industry. A finance lease is a transaction styled as a lease which enables the lessee to purchase the vessel at the conclusion of the lease for a nominal amount. Current law treats these arrangements as conveyances of title subject to an obligation to pay for the conveyance over time. The obligation is deemed secured by a lien on the property. On the other hand, an owner may charter a vessel under what he believes is a bona fide charter and include an option to purchase which may be very favorable to the charterer. Through inadvertence, the charter with the purchase option could be so favorable to the charterer that it would be treated by a court as being equivalent to a finance lease which has conveyed title to the vessel. This would mean that from the moment the charter was signed, the vessel was improperly documented, which could subject the owner to statutory penalties, and it would also mean that the "owner's" interest in the vessel, which has been transformed into a security interest, is unperfected. The Uniform Commercial Code deals with this problem by permitting equipment lessors to protect themselves by having the nominal lessee sign a financing statement "for informational purposes" and file it where one would otherwise file a financing statement to perfect a security interest in property owned by the lessee. Then, if a court deems the transaction to be a conveyance of title, the informational financing statement is effective to perfect the interest of the unwitting seller. The ABA subcommittee's draft contains a provision, § 31322(c), which would allow an owner of a vessel to file an informational notice of mortgage pertaining to a charter which would have the effect of perfecting a security interest in the vessel in the event the charter were deemed to be a conveyance of the vessel.

5. At § 31322(d), the ABA subcommittee draft adopts the view expressed by Gilmore & Black in The Law of Admiralty, 2d Ed., p. 729, that when equipment subject to a purchase money security interest under the Uniform Commercial Code (or otherwise applicable state law) becomes an appurtenance to a vessel, it is inequitable for an existing preferred mortgagee of a vessel to attain priority over the holder of the security interest, who gave new value. It would be a windfall for the existing preferred mortgagee to get the benefit of the additional equipment as collateral when a subsequent lender furnished it. In the ABA

subcommittee's draft, however, this has been restricted to equipment that is readily removeable without substantial damage to the vessel. A good argument could be made to apply the principle against all maritime lienholders in existence at the time equipment is placed aboard the vessel, although the ABA subcommittee's draft does not go that far.

6. The ABA subcommittee's draft makes clear at § 31322(f) that a preferred mortgage may secure any obligation of the mortgagor, "whether absolute or contingent, direct or indirect, existing at the time the mortgage is executed or arising thereafter, or liquidated or unliquidated." From time to time there have been questions raised whether a mortgage can be used to secure a shipowner's obligation under a guaranty of another's debt, for example, and this section puts to rest all such questions.

7. At § 31322(g), the ABA subcommittee's draft suggests making it explicit that preferred mortgages may be subordinated, and that the subordination agreement may be made a part of the public record of the vessel just like mortgages themselves.

8. Existing law permits a preferred mortgage to cover more than one vessel, or to cover a vessel and non-maritime property. In the case of a mortgage covering more than one vessel, unless the mortgage explicitly provides for its own formula, 46 U.S.C. § 922(f) provides a formula to determine the amount of the debt that must be repaid in order to discharge one of the vessels from the mortgage. In the case of a mortgage that covers a vessel and non-maritime property, however, the Ship Mortgage Act currently states, at 46 U.S.C. § 922(e), that the mortgage must state a separate discharge amount for the non-maritime property. There would appear no reason in principle why there should be a different approach in the two situations, and at § 31322(h), the ABA subcommittee draft adopts the approach currently used in fleet mortgages for both situations.

9. As drafted by the ABA subcommittee, § 31322(i) would codify the principle acknowledging the sufficiency of substantial compliance with the provisions of the Ship Mortgage Act. While this principle is currently developing in case law, courts occasionally require strict compliance. There is no suggestion in the Ship Mortgage Act that a rule of strict compliance was the intention of the Congress in enacting the law, and I recommend codifying the principle and a recognition that it is a codification of the original intention of Congress.

10. The ABA subcommittee's suggested § 31324(c) codifies the principle in the case of The OCONEE, 280 F. 927 (E.D. Va. 1922), which makes it clear that if a shipowner or vessel's master does not keep a copy of a mortgage aboard the vessel and exhibit it to any interested parties as required, this will not affect the preferred status of the mortgage.

11. Under existing law, the district courts have jurisdiction only to foreclose a preferred mortgage and seek a deficiency judgment against the shipowner, see 46 U.S.C. 954(a). Guarantors or other persons liable for the same debt must be sued in a separate action in state court unless some other basis for federal jurisdiction exists, which is not always the case. This has two undesirable effects: First, it leads to a multiplicity of legal actions to collect what is essentially the same obligation. Second, because guarantors are not now proper parties in these cases, it prevents guarantors from having a practical means of protecting their interests in the case which will sell a vessel and, as a practical matter, determine the amount of the deficiency which will be sought against the guarantors. At § 31325(b)(2), the ABA subcommittee's draft would extend federal jurisdiction in a foreclosure case to guarantors and other individuals obligated on the mortgage debt.

12. Existing law provides that a district court may appoint a receiver for a mortgaged vessel and authorize the receiver to operate the mortgaged vessel using the proceeds to help discharge the mortgage debt, see, 46 U.S.C. 952. This provision is rarely used, because mortgagees have a concern that if the receiver allows the vessel to be operated outside the territorial limits of the judicial district in which the vessel has been seized, the district court that seized the vessel would lose its jurisdiction over the vessel. At § 31325(e)(1), the ABA subcommittee's draft makes clear that the district court would not lose jurisdiction in that instance. This would provide protection in receivership cases, at least unless the vessel were taken to a foreign country.

13. At § 31326(b)(1), the ABA subcommittee's draft provides that all amounts secured by the mortgage, even amounts advanced after the mortgage is granted, enjoy the priority of the preferred mortgage as of the moment it is perfected as a preferred mortgage. In essence, this means that even discretionary future advances under a preferred mortgage would, for priority purposes, be treated the same as advances made at the time the mortgage is granted.

14. Under current law, a foreign lender may enjoy the benefit of a preferred mortgage on an American vessel if the mortgage is held in trust for the lender by an approved trustee under 46 U.S.C. §§ 808 and 961(e). Under current agency practice, however, unlike other mortgagees, a mortgage trustee for a foreign lender may not use the mortgage debt to purchase the vessel at a judicial foreclosure sale. It is also generally accepted that the Maritime Administration lacks the authority to authorize these trustees to purchase at a foreclosure sale. The right of a mortgagee to bid the mortgage indebtedness for a vessel, and to purchase the vessel at a foreclosure sale is vital to full realization on the mortgage debt. A foreclosure sale is a cash sale, which almost invariably depresses the sale value of a vessel below its true value. It is important that a lender be able to purchase the vessel at a sale, and resell it later for a higher price, thereby recouping some of all of its deficiency. The inability of a foreign lender, even through a trustee, to avail itself of this right is of great concern to foreign lenders. Many U.S. lenders have suffered enormous losses in financing vessels in recent years, some to the point that they now completely shun vessel financing opportunities. To a large extent, foreign lenders have, often eagerly, been filling this void, especially in the fishing industry in the North Pacific. Many foreign lenders, however, are greatly concerned about the inability to acquire, directly or through their mortgage trustees, the financed vessels at foreclosure sales. This has chilling effects on financing transactions which could tend to restrict the amount of capital available to the U.S. maritime industry. At § 31329(d), the ABA subcommittee draft makes a proposal that a mortgage trustee for a foreign lender may be a purchaser of an American vessel at the foreclosure of the mortgage it holds in trust provided the vessel is not documented in the name of the trustee and is not operated in any trade. This would enable the foreign lender to get the full benefit of its security in the vessel, and yet would insure that the vessel, while owned by the trustee for the benefit of the foreign lender, would not be traded in competition with American operators. The existing provisions of the Shipping Act, 46 U.S.C. §§ 808 and 835, will forbid the trustee as owner from selling the vessel or chartering the vessel to a foreigner without obtaining the approval of the Maritime Administration. The ABA subcommittee's suggested language would also make clear that a vessel so purchased by the trustee and later resold to an American citizen would not lose any of its trading privileges, such as the privilege of engaging in the coastwise trade. It is common for mortgage trustees to hold both the note or bond and the mortgage securing it in trust, although often the trustees are used to hold only the mortgage. Unlike other proposals on the issue of mortgage trustees purchasing vessels at foreclosure sales, the

ABA subcommittee's draft does not limit the availability of the right to trustees who hold only the mortgage in trust. There is no reason in principle to distinguish the two instances.

15. As a related provision, the ABA subcommittee has also suggested amendments to 46 U.S.C. §§ 808 and 835 which would confer on the Maritime Administration the authority to permit one who is not a citizen of the United States to purchase a vessel at a judicial sale. Thus, in instances in which it would not be contrary to the national interest for a vessel to be acquired by a non-citizen, the available pool of bidders at foreclosure sales would be increased in some instances, which could improve the realization on the secured debt by lenders, and would reduce the deficiency owing by the applicable shipowners.

16. As a recodification of 46 U.S.C. § 971, which confers a lien to those who furnish necessaries to a vessel, § 31342 of H.R. 3105 uses as its operative language the notion of "providing" necessaries "for" a vessel, whereas existing law speaks of "furnishing" necessaries "to" a vessel. This would constitute a major change in existing law. As a general rule, under existing law the supplier of necessaries is conferred a lien only if the necessaries actually reach the vessel. There is no lien, for example, if supplies are purchased with the intention of their being used on a particular vessel, but never leave the shipowner's warehouse on shore. The change from "furnishing to" to "providing for" would encourage the argument that the intent that necessaries be placed aboard a vessel would be sufficient whether or not the necessaries actually reached the vessel. The ABA has suggested corrective language at § 31342.

17. Throughout H.R. 3105, the ABA draft changes the phrase "civil action" to "civil case." This has been done to conform the language to that used in 28 U.S.C. § 1333(1), the grant of admiralty jurisdiction to the district courts. A considerable amount of jurisprudence has developed construing the difference between civil actions and civil cases under Title 28. This change in usage will avoid the argument that the proceedings could be construed as "federal question" cases of an "admiralty" or "*in rem*" nature, depriving litigants in these cases of the unique provisions of the federal rules for admiralty cases. (In this regard, the Ship Mortgage Act refers to "suits" and "suits *in rem* in admiralty." If the usage in H.R. 3105 is not changed to "cases," we suggest that it be changed to "suits" instead of retaining the existing language of H.R. 3105.)

The recodification of the Ship Mortgage Act presents a unique opportunity to correct existing and anomilies in the law, streamline vessel financing, reduce the cost of obtaining financing to shipowners, and reduce the administrative burdens the act places on the Coast Guard. The maritime financing community deeply appreciates the interest of your subcommittee in tackling these issues, and would like to assist this subcommittee in any way that it can.

Thank you for this opportunity to testify on this important piece of legislation.

NOTICE OF MORTGAGE

SHIPOWNER: ______________________________

MORTGAGEE: ______________________________

MORTGAGEE'S ADDRESS:

____

____

____

VESSEL NAME: ____________________ OFFICIAL NO. ________

PRINCIPAL AMOUNT OF MORTGAGE ____________________

COLLATERAL DESCRIPTION: ____________________

____

____

____

____

____

Check, if applicable:

_____ This notice of mortgage is filed with respect to the above-described ~~col~~lateral for informational purposes in connection with a charter thereof by the above-named shipowner in favor of the above-named mortgagee.

SIGNATURE OF SHIPOWNER: ____________________

____

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September 15, 1988

The Honorable Walter B. Jones
Chairman
Committee on Merchant Marine and Fisheries
1334 Longworth Building
U. S. House of Representatives
Washington, D. C. 20515-3301

Re: HR 3105 - Proposed Recodification of Ship Mortgage Act

Dear Congressman Jones:

The Section of Business Law of the American Bar Association respectfully requests that the testimony of Bruce A. King presented to the Subcommittee on Merchant Marine and Fisheries June 28, 1988 on the proposed recodification of the Ship Mortgagage Act - HR 3105 be recorded as the position of the Section of Business Law. Mr. King's testimony was developed by the Section's Subcommittee on Maritime Financing and was adopted by the Section August 10, 1988.

This position is presented only on behalf of the Section of Business Law. It has not been considered or approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the position of the Association.

I, on behalf of the Section, urge your careful consideration of the recommendations in the testimony because they have been carefully prepared by knowlegeable practitioners in this area of the law. If you or any members of your Committee desire further information about the issues, Mr. King or members of his subcommittee would be pleased to make themselves available to the Committee.

Very truly yours,

David E. Nelson

David E. Nelson

cc: George E. Bushnell
Chairman, ABA House of Delegates

Walter H. Beckham
ABA Secretary

Robert D. Evans
Director, ABA Governmental Affairs Group

Anita Connelley
Staff Assistant, ABA Office of Policy Administration

U.S. Department of Transportation

General Counsel

400 Seventh St., S.W.
Washington, D.C. 20590

DEC 8 1986

The Honorable Walter B. Jones
Chairman, Committee on Merchant
Marine and Fisheries
House of Representatives
Washington, D.C. 20515

Dear Mr. Jones:

I refer to your request for the views of the Department of Transportation regarding H.R. 3158, a bill

> To revise, consolidate, and enact certain laws related to maritime commercial instruments and liens and public vessels and goods as chapters 313 and 315 of title 46, United States Code, "Shipping".

H.R. 3158 would codify chapters 313 and 315 of title 46, United States Code, "Shipping." This bill is the result of a drafting effort of the Law Revision Counsel. The bill would update the laws on maritime commercial instruments, liens, public vessels and goods. The Department supports the revision effort.

We believe there should be an additional subchapter relating to court actions involving liens on vessels. The provisions of sections 31325(b)-(e), 31326(b), 31328, and 31344 should be rearranged and included in the new subchapter. We have included a draft of the new subchapter.

We note that there does not appear to be any coordination between H.R. 3158 and H.R. 440, making amendments to the Federal Tort Claims Act.

You should also be aware that the International Maritime Organization (IMO), the Comite' Maritime International (CMI), and United Nations Conference on Trade and Development (UNCTAD) are presently considering the question of maritime liens and mortgages. Any substantial changes in this area, agreed to by the international maritime community, could have an impact on the domestic law relating to maritime liens and mortgages.

The Department has a number of comments (enclosed) which were prepared in cooperation with the technical experts in the Coast Guard and the Maritime Administration.

The Office of Management and Budget has advised this Department that there is no objection to the submission of this report from the standpoint of the Administration's program.

We appreciate the opportunity to comment on this bill.

Sincerely,

Jim J. Marquez
General Counsel

Enclosure

COMMENTS ON H.R. 3158

I. Chapter 313 Commercial Instruments and Maritime Liens

SUBCHAPTER I -- GENERAL

Section 31301(2), page 2, line 14: To make this a complete definition of mortgagee, insert after mortgagee "means a person to whom property is mortgaged or".

Section 31301(2), page 2, line 15: In cases involving trust deeds and bond issues, there are numerous bonds issued; accordingly, the word "issued" should be replaced with "issue" as it currently appears at 46 App. U.S.C. 911(5).

Section 31301(5)(B), page 3, line 13: To be consistent with line 10, the phrase "hypothecation, or similar charge" should be inserted after "mortgage".

Section 31302, page 3, line 23: As presently drafted, this section does not provide for the Secretary to furnish certificates of ownership ("1330's"). Such certificates are important for determining the status of recordings with the Coast Guard. The phrase "or a record" should be inserted after "copy".

Section 31302(c), page 3, line 25: As presently drafted this section does not specifically provide the Secretary with authority to prescribe fees for endorsing documents. The phrase "endorsing documents" should be inserted after "instruments,". However, if our suggestion on page 6 to eliminate endorsements is accepted, this change is unnecessary.

Section 31302(d), page 3, line 29: The grantor acknowledges a deed; the notary or other authorized official takes the grantor's acknowledgment. The phrase, "to acknowledge deeds" should read, "to take acknowledgment of deeds".

Section 31304(a)(1), page 3, lines 37-39: This should be omitted. We see no reason for a special provision for liability due to government mistakes, aside from what may now exist in other laws. In addition, because of the use of the term "Secretary", this provision appears to broaden the government's exposure compared to the existing provisions. (Even the existing provisions are somewhat open-ended, since there are no standards for the Secretary's performance of various duties.)

Section 31304(b), page 4, lines 6-7: The provision that authorizes award of costs and attorney's fees should be omitted. The Equal Access to Justice Act provides that certain parties who prevail over the federal government in litigation are entitled to an award of attorneys' fees and expenses unless the government can demonstrate that its position was substantially justified or special circumstances would make an award unjust.

Section 31307, page 4, line 24: To provide adequate regulatory authority, the word "and" should be deleted and the phrase "and notices of claims of liens and other instruments" should be inserted after "assignments".

SUBCHAPTER II -- COMMERCIAL INSTRUMENTS

Section 31321(d)(1), page 5, line 12: While present law seems to require filing of partial discharges, the provision is almost universally ignored. This section should allow mortgagors the option of filing or not filing partial discharges. Also, a mortgage is satisfied when the mortgagor pays the indebtedness or otherwise complies with the terms of the mortgage; thereupon, the mortgagee provides a written notice of the discharge. Lines 12 through 15 of this subparagraph should read as follows:

> Upon discharge in whole or part of indebtedness under a mortgage recorded under this section, a mortgagor may provide the Secretary with a written acknowledged certificate of discharge of the indebtedness. The Secretary shall record the certificate.

Section 31322(a), page 5, line 23: The phrase should read: "A preferred mortgage is a valid mortgage", as the present statute does. Many courts have used this language in their decisions.

Section 31322(a)(3) should be deleted. See comment on section 31322(b).

Section 31322(a)(5), page 5, line 30: The affidavit is a useless, time consuming formality. The words "is accompanied by an affidavit that the mortgage" should be deleted.

Section 31322(a)(6), page 5, lines 33 & 34: This should be omitted. We see no reason to withhold all preferred status from a mortgage merely because it contains a partial waiver of preferred status (e.g., it subordinates itself to certain potential lienors' liens). If it completely waives its preferred status, then it seems a misnomer to call it a preferred mortgage, but it is still recordable under section 31321. A well-known authority comments on the existing identical provision: "On the face of it, this seems an idiotic statement; indeed it is an idiotic statement." Gilmore & Black, The Law of Admiralty (2d ed.) 711.

Section 31322(a)(7)(A), page 5, line 36: "State" is not defined. That is no problem if chapter 313 is codified under subtitle II of Title 46, which defines "State" at section 2101(36) or if that definition is moved to a title-wide definition section; if not, a definition should be added at section 31301 or elsewhere.

Section 31322(a)(7)(C), page 5, lines 38 & 39: The words "under the first section" and "801" should be deleted, since "citizen of the United States" is not defined in the first section of the Shipping Act, 1916 (46 App. U.S.C. 801) and reference to that section would therefore be dangerously confusing.

Section 31322(a)(7), page 5: To make explicit that the United States may be a mortgagee, as has been held by the courts, a provision (D) should be added: "(D) the United States".

Section 31322(b), page 5, line 41: When a mortgage covers additional property other than a vessel, present law denies the mortgage preferred status if it fails to state a separate discharge amount for the additional property. This consequence is both severe and unnecessary. The problem can be cured by providing a statutory discharge formula, as is done for mortgages covering more than one vessel (see section 31322(e)). The words after "vessel" should all be deleted and the following should be inserted: "and the mortgage fails to provide for the separate discharge of the additional property by paying a specified part of the mortgage indebtedness, all such additional property shall be discharged from the lien of the mortgage by the payment of .01 percent of the total amount of the mortgage. The failure to include the separate discharge of the additional property shall not affect the preferred status of the mortgage." Incidentally, this subsection would be more logically placed before subsection (e).

Section 31322(d)(6), page 6, line 13: If section 31322(d) is not deleted as recommended, the word "vessel" should be "additional property" for consistency with section 31322(b). To be consistent with the change in section 31322(b), the words "as provided ... section" should be deleted and the following inserted: "when the mortgage covers a vessel and additional property that is not a vessel, if specifically provided in the mortgage." Alternatively, language parallel to section 31322(d)(7) should be used.

Section 31322(e), page 6, line 21: The current draft uses the word "attributable" to replace existing statutory language, and in doing so leaves much unsaid. This can be cured by adding to the end of the section: "Upon payment of that amount, the vessel shall be discharged from the mortgage."

Section 31322: The following new subsection should be added after subsection (a) or subsection (e): "A preferred mortgage may secure indebtedness, revolving lines of credit, guarantees or contingent liabilities. For the purposes of section 31321 (c)(2)(E) and subsection (d)(4) of this section, the amount of the mortgage is the principal portion of the maximum amount of potential liability."

Section 31322 (a)(4), (d), and (f), page 5, line 29, and page 6, lines 5-17 and 24-26: The requirement that the certificate of documentation be endorsed in order for the mortgage to attain preferred status imposes on the industry the significant burden of recording and endorsing the document on the same day in order to perfect a security interest. This can lead to considerable problems and expense, especially when the vessel is engaged in foreign trade or a large number of vessels are involved in a single transaction. To relieve the industry of this burden, the requirement for endorsement should be eliminated by deleting sections 31322(a)(4), 31322(d), and 31322(f). The purpose of the requirement is to give notice of the preferred mortgage to later potential lienors. Such persons can obtain the same information from the vessel documentation office. In this era of rapid, convenient communications, endorsement of the document is unnecessary. Eliminating it would relieve the industry of a troublesome burden, and eliminate the Coast Guard's endorsement task.

To complete this change, three other provisions should also be changed: section 31321(d)(2), page 5, lines 16-21 should be deleted; section 31322, our recommended new subsection (which describes types of obligations which a preferred mortgage may secure) contains a reference to section 31322(d)(4) which should be deleted; section 31323(b), page 6, lines 33-34 should be amended by deleting "and have endorsements about the mortgage put on the vessel's certificate of documentation".

Section 31324, page 7, lines 5 & 8: Restriction of subsection (b) to self-propelled vessels is new and unwarranted. The word "self-propelled" should be deleted from (b) and from the section title.

Section 31325(b)(1), page 7, line 18: This subsection should provide for an action *in rem* and/or an action *in personam*. The word "and/" should be added before "or" to insure that the remedies are considered conjunctive and disjunctive.

Section 31325(d)(1), page 7, line 29: We recommend the present statutory language be included: "other ranking officer or caretaker". Alternatively, the term "master" should be deleted, leaving only "individual in charge".

Section 31325(d)(3), page 7, lines 36 - 37: The mortgagee should only be liable for damages when he fails to provide a required notice. As drafted, the mortgagee is held liable for not providing notices that are not required. The second sentence should read: "However, when the notice required by this subsection is not given, the mortgagee ... damages in an amount not more than that person's interest in the vessel ..."

Section 31325(d)(3), page 8, lines 2-3: The costs and attorney's fee provision should be deleted. (See comments on § 31304(b).)

Section 31325(e), page 8, line 6: After the words "mortgaged vessel", the following should be added: "and shall retain _in rem_ jurisdiction over the vessel even if the receiver operates the vessel outside the district in which the court is situated".

Section 31326(a), page 8, line 14: The term "prior" is superfluous, since the vessel is sold free from any claim. The use of any modifier to the word "claim" can create confusion. The term in present law is "preexisting." In the context of this statute, a prior claim would normally mean a claim having priority. That is the wrong meaning in this context. We recommend that the word "prior" be deleted; the words "preexisting at the date of sale" could be added after "vessel." The language of the subsection could be improved by making it parallel to the language of section 31344, by inserting a phrase after the word "title" to read: "the vessel shall be sold free of any claim in the vessel preexisting at the date of sale, including a possessory common law ...".

Section 31328, page 8, line 32: The phrase "a mortgage covering" should be deleted.

Section 31329(a), page 8, line 41: The words "or a substitute trustee" should be added after "trustee".

Section 31329(a)(3), page 9, line 4: Only a citizen of the United States as defined in section 2 of the Shipping Act, 1916 can be an approved trustee. The words "within the meaning of section 2 of the Shipping Act, 1916 (46 App. U.S.C. 802)" should be added at the end of the sentence. Likewise, the same words should be added after "United States" on page 8, line 40.

Section 31329(b), page 9, line 9: The words "or a substitute trustee" should be added after "trustee".

Section 31329(c), page 9, line 11: The words "issued, transferred or" should be inserted after "be".

Section 31330, page 9, line 25: In conjunction with deletion of the affidavit of good faith from section 31322(a)(5), the following should be added: "or with intent to hinder an existing or future creditor of the mortgagor or a lienor of the vessel, records with the Secretary a mortgage made not in good faith".

SUBCHAPTER III -- MARITIME LIENS

Section 31341(a)(3), page 9, line 36: The terms "ship's husband" and "operator" should be included. These terms were in the existing law.

Section 31341(b), page 10, line 2: The word "improperly" expands the existing provision. We recommend the existing statutory language: "tortiously and unlawfully" vice "improperly".

Section 31343(a), page 10, line 15: When a person records a notice of claim of lien, a copy should be provided to the vessel owner so the owner will be aware of the filing and can have it deleted from the record when the lien is paid off. The second sentence should be amended to read: "To be recordable, a copy of the notice must be provided to the owner of the vessel and the notice must -".

Section 31343(c), page 10, lines 23-26: The person having the claim is not generally the person who discharges it. The words "On Discharging" should be replaced with "On discharge of ".

Section 31344, page 10, lines 28 - 30: The suggestion that a preferred maritime lienor cannot have a vessel sold free of all claims should be eliminated. A clear statement of present statutory and case law can be made by deleting the words "covered by a preferred mortgage" and "(except a preferred maritime lien)". The following words should then be inserted on line 31 after "However": "when the vessel is covered by a preferred mortgage and the maritime lien being enforced is not a preferred maritime lien,".

Section 31344, page 10, line 30: The word "prior" should be deleted; the words "preexisting the date of sale" could be added after "vessel". (See comment on section 31326(a) above.)

Section 31344, page 10, line 31: A mortgagee should not be required to accept a mortgage with a new debtor without the mortgagee's consent. The words "plaintiff, or intervenor" should be deleted. This is a substantive change, and expected to be noncontroversial.

Section 31344, page 10: Current law requires notice in the case of foreclosure on a mortgage, but not foreclosure on a lien. Notice should be provided in both cases. Existing language in section 31344 should become (a) and a new subsection should be added, as follows:

(b)(1) Actual notice of a civil action brought under section 31342(2) must be given in the manner directed by the court to -

(A) the master, caretaker, other ranking officer, or individual in charge of the vessel; and

(B) any person that has recorded under section 31343(a) of this title a notice of claim of lien on the vessel or a mortgage under section 31321(a).

(2) [same as section 31325(d)(2)]

(3) [same as section 31325(d)(3) as amended].

Section 31345, page 11, lines 1-4: The existing provision applies to the entire chapter. This provision should be placed in subchapter I and applied to "this chapter."

SUBCHAPTER IV. COURT ACTIONS INVOLVING PREFERRED MORTGAGE AND MARITIME LIENS

Section 31361. Enforcement of preferred mortgage liens [replacing section 31325(b)-(e)]

(a) On default of any term or condition of a preferred mortgage on a vessel, the mortgagee may enforce the preferred mortgage lien by bringing --

(1) a civil action _in rem_ in admiralty; and/or

(2) a civil action _in personam_ in admiralty against the mortgagor for the amount of the mortgage indebtedness secured by the mortgaged vessel or any deficiency in paying off that indebtedness.

(b) The district courts of the United States have --

(1) original jurisdiction, exclusive of the courts of the States, of a civil action brought under subsection (a)(1) of this section; and

(2) original jurisdiction of an action brought under subsection (a)(2) of this section.

(c)(1) Actual notice of a civil action brought under subsection (a)(1) of this section must be given to --

(A) the master, caretaker, or individual in charge of the vessel; [see comments on section 31325(d)(1)]

(B) any person that has recorded under section 31343(a) of this title a notice of a claim of an undischarged lien on the vessel and to a mortgagee of a mortgage or assignment of a mortgage recorded with the Secretary.

(2) With permission of the court, actual notice under this subsection is not required if the person entitled to the notice cannot be found in the United States.

(3) Failure to give actual notice required by this subsection does not affect the jurisdiction of the court in which the civil action is brought. However, when the notice required by this subsection is not given, the mortgagee is liable to a person not receiving notice for damages in an amount not more than that person's interest in the vessel terminated by the action brought under subsection (a)(1) of this section. A civil action may be brought to recover the amount of the terminated interest. The district courts of the United States have original jurisdiction of the action, regardless of the amount in controversy or the citizenship of the parties.

(d) In a civil action brought under subsection (a)(1) of this section --

(1) the court may appoint a receiver and authorize the receiver to operate the mortgaged vessel and shall continue to retain *in rem* jurisdiction over the vessel even if the receiver operates the vessel outside the district in which the court is situated; and

(2) when directed by the court, a United States Marshall may take possession of a mortgaged vessel even if the vessel is in the possession or under the control of a person claiming a possessory common law lien.

Section 31362. Court sales to enforce preferred mortgage liens and priority of claims [replacing section 31326]

(a) When a mortgaged vessel is sold by order of a district court of the United States in a civil action brought under section 31361(a)(1) of this title, the vessel shall be sold free of any claim preexisting at the date of sale, including a possessory common law lien of which a person is deprived under section 31361(d)(2) of this title.

(b) Each of the claims terminated under subsection (a) of this section attaches, in the same amount and priority, to the proceeds of the sale, except that --

(1) the preferred mortgage lien has priority over all other claims against the vessel (except for expenses and fees allowed by the court, court costs, and preferred maritime liens); and

(2) for a foreign vessel, the preferred mortgage lien is subordinate to a maritime lien for necessaries provided for the vessel in the United States.

Section 31363. Court sales to enforce maritime liens [replacing section 31344]

(a) When a documented vessel is sold by order of a district court of the United States to enforce a maritime lien, the vessel shall be sold free of all claims preexisting at the date of sale. However, on request of the mortgagee, the court shall require the buyer to give, and the mortgagee to accept, a new mortgage on the vessel for a period of time equal to the time remaining under the original mortgage. To the extent practicable, the conditions of the new mortgage shall be the same as those of the original mortgage, and the new mortgage is subject to approval by the court. When a new mortgage is given, the existing mortgage may not be paid from the proceeds of the sale, and the amount payable as the buying price shall be reduced by the amount of the new mortgage indebtedness.

[(b): would be the same as proposal for new subsection (b) in section 31344]

Section 31364. Forfeiture of mortgage interest [replacing section 31328].

The interest of a mortgagee in a documented vessel may be terminated by forfeiture of the vessel for a violation of a law of the United States only if the mortgagee authorized, consented, or conspired to do the act, failure, or omission that is the basis for the violation.

[Section 31325(a) would become "section 31325. Preferred mortgage liens". Section 31325(b)-(e) would be deleted. Sections 31326, 31328, and 31344 would be deleted.]

II. Chapter 315 of title 46 U.S.C. - Public Vessels and Goods.

In our opinion, chapter 315 is seriously flawed. The general purpose of this chapter appears to be to recodify, in a more rational form, the present confusing mix of statutes dealing with government claims and litigation, the Federal Torts Claims Act, 28 U.S.C. 2671-2680 (and 28 U.S.C. 2401), the Extension of Admiralty Act, 46 U.S.C. 740, the Suits in Admiralty Act (SIAA), 46 U.S.C. 741-752, and the Public Vessels Act (PVA), 46 U.S.C. 781-791. This is a worthy purpose. But the proposed chapter fails to accomplish that purpose. In so doing, it opens up whole new difficulties.

We have a number of specific comments.

SUBCHAPTER II -- ACTIONS AGAINST THE UNITED STATES GOVERNMENT

Section 31513. Time and place for claims and actions.

This section creates a confusing statute of limitations which is not consistent with any of the statutes cited above.

Section 31516 Defenses and remedies.
This section is inconsistent with all of the statutes cited above, and threatens to overturn defenses currently available to the Government under the admiralty statutes. The results of this would be disastrous.

Section 31518. Judgments against the United States.

This section provides for interest in judgments against the Government. Nowhere in the chapter is there any provision for interest in judgments for the Government.

Furthermore we have the following general comments:

1. The Discretionary Function Exception:

a. The most serious flaw is in section 31516, and in the lack of appropriate exceptions to liability found in the Federal Torts Claims Act (FTCA) at 28 U.S.C. 2680. The most important of these is the 2680(a) exception for "discretionary functions," which has been given broad and significant reading in the recent Supreme Court case of *United States v. S.A. Empresa de Viacao Aerea Rio Grandense (Varig Airlines)*, 104 S.Ct. 3755 (1984). A number of the Federal Circuits have read the discretionary function exception into the admiralty statutes, none of which have contained any such explicit exceptions to liability, by reasoning that the specific provisions in the FTCA were a Congressional codification of an existing principle. *Bearce v. United States*, 614 F. 2d 556 (7th Cir. 1980). cert. den. 449 U.S. 837 (1980); *Canadian Transport Co. v. United States*, 663 F. 2d 1081 (D.C. Cir. 1980); *Garvey v. United States*, 663 F. 2d 1081 (D.C. Cir. 1980); *Gercey v. United States*, 540 F. 2d 536 (1st Cir. 1976), *cert. den.* 430 U.S. 954 (1977). At least one of these cases, *Canadian Transport*, recognized a basis for the discretionary function exception in Constitutional Separation of Powers. Most if not all of the cases, however, have given great weight to the idea that the FTCA statutory exceptions were a codification of preexisting common law principles, excusing the lack of a similar codification of such exceptions under the admiralty statutes because of their more ancient lineage. (This is the line of analysis which presently finds the best support from the Supreme Court in the *Varig* case.) This whole line of analysis will be undercut if the admiralty statutes are now completely recodified, with the noticeable omission of the FTCA exceptions, and worse yet, with a specific section entitled "Defenses and Remedies" which omits reference to any such exceptions.

b. This proposal could do grievous harm to the Coast Guard and to other agencies such as the Corps of Engineers which are exposed to a maritime liability. A typical aids-to-navigation case may illustrate the point. If a vessel casualty occurs because a buoy is off station, and it is shown that the Coast Guard was negligent in allowing that buoy to drift off station, the Coast Guard will be liable for that "operational negligence." This is a reasonable rule of law, and one that the Coast Guard can deal with in a straightforward manner by simply doing its best to respond to aids-to-navigation discrepancies in a competent manner. Absent the protection of the discretionary function exception, however, a plaintiff is free to sue the Coast Guard for a casualty occurring near an on station buoy, arguing that the planners in the district aids-to-navigation branch should have established two buoys, or a fixed light instead of a buoy. The plaintiff is free to demand testimony and documents from the officers responsible in the district aids-to-navigation branch in order to pursue a detailed inquiry into their reasons for not doing so. This is what the discretionary function exception, as understood by most of the Circuits, protects against. Absent this protection, our exposure to liability is increased manyfold; as is our exposure to litigative harassment, even in those cases which we may eventually win.

c. This defect could be dealt with quite simply by insertion of the following sort of language into section 31516, incorporating by reference both the FICA and the common law:

> (a) The United States Government is not subject to suit under this subchapter for any matter excepted in 28 U.S.C. 2680 from the provisions of 28 U.S.C. chapter 171 and 1346(b), or which arises from uniquely governmental functions. In addition, the United States Government may limit its liability and use any defense available to a private person.

2. Other provisions:

a. Time limitations. There are currently three different time limitation rules:

(1) Under the FTCA, one must first present an administrative claim within two years, and then bring suit within six months of a formal denial of that claim. Once an administrative claim is filed under the two years, the claimant and the government have an unlimited amount of time to negotiate, if both are willing. This had the virtue of allowing for quite a bit of flexibility in the handling of claims, while still insuring that the Government has fair notice. These provisions are widely known by private attorneys dealing with the Government.

(2) Under the SIAA and the PVA, suit must be filed within two years. Administrative claims are irrelevant. It is a simple rule.

(3) Under the Extension in Admiralty Act, one must meet the same absolute two year limit for suit as in the SIAA and the PVA, but must also wait until six months after filing an

administrative claim. This means that filing an administrative claim after one year and six months would preclude initiating a suit if the agency does not take action on the claim within the remaining six months. It is a confusing rule that almost no one understands.

(4) Under the proposed section 31513, the rule in all admiralty cases would be the same as it is now under the Extension in Admiralty Act, except that the suit limit would be three instead of two years, and the last chance to get in an administrative claim would be two and one half instead of one and one half years. Having such a confusing rule applied to all admiralty cases could cause the courts to tinker with time limitations. One way in which they might be tempted to do so, among many others, is via the inartful language in section 31532 on counterclaims. Section 31532 should specifically provide that it does not give rise to a claim otherwise barred by section 31513.

(5) In addition, strong consideration should be given to not lengthening the present two year limits found in the FTCA and the admiralty statutes. It has been our experience that it is extremely difficult to recover documentation and locate witnesses in cases (or claims) which first come to our attention near the end of the limitations period. The nature of governmental organization generally makes it difficult to identify potential claims and litigation in advance in order to take steps to preserve evidence. The military charter of the Coast Guard, with periodic transfers and retirements, makes it difficult to locate and provide witnesses.

b. Interest. Section 31518 brings up the matter of interest. But there is no recognition of the right of the Government to collect interest beginning at the time of suit. There is no recognition of the traditional right of interest from the time of loss in certain types of cases. Geotechnical Corp. of Delaware v. Pure Oil Co., 214 F. 2d 476 (5th Cir. 1954). Also there is no indication of how this chapter is intended to mesh with the provisions of the Federal Claims Collection Act, at 31 U.S.C. 3717 (as amended by Pub L. 97-452, 1983) or the extent to which contract claims may be subject to the interest provisions of the Contract Disputes Act of 1978 (41 U.S.C. 601 et. seq.).

SUBCHAPTER III -- ACTIONS BY THE UNITED STATES GOVERNMENT

Section 31532. Counterclaims, cross-claims, and credits.

This section might be read to allow counterclaims based on actions otherwise time barred.

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May 16, 1986

John Cullather, Esq.
Merchant Marine and Fisheries Committee
United States House of Representatives
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Re: H.R. 3158 - Proposed Recodification
of Title 46 United States Code Dealing
with Ship Mortgages and Maritime Liens

Dear Mr. Cullather:

Proposed H.R. 3158 (hereinafter "H.R. 3158") has been reviewed by the Marine Finance Committee (the "Finance Committee") of the United States Maritime Law Association for the purpose of pointing out any substantive changes that may have been made to the law as it exists today in Title 46 of the United States Code (provisions of Title 46 of the United States Code as presently in effect are hereinafter referred to as the "Current Statute").

In reviewing H.R. 3158 and preparing the within comments, the Finance Committee also considered the discussions which took place at the meeting held on June 13, 1985 between representatives of the special subcommittee (the "Subcommittee") of the Finance Committee and you, Mr. Monaco and Mr. Kelly (the "Drafters") regarding an earlier draft of the proposed recodification (hereinafter the "Draft Proposal").

After reviewing H.R. 3158 with the above considerations in mind, the enclosed chart was prepared. The left hand column of the chart contains H.R. 3158, the next column contains the corresponding section of the Draft Proposal, the third column contains the provisions of the Current Statute upon which the Draft Proposal and H.R. 3158 are based and the right hand column contains the comments which resulted from such review.

This chart was circulated to the members of the Finance Committee at its October 30, 1985 meeting, at which time it was noted that many of the comments made by the Subcommittee to the Drafters at the June 13th meeting had been incorporated in H.R. 3158 but that H.R. 3158 still posed certain significant problems, discussed below. In addition, several members of the Finance Committee made additional comments at the October 30th meeting. These comments have been incorporated in the chart and are footnoted to reflect that they were added subsequent to the chart having been circulated.

A report of the action taken by the Finance Committee in respect of H.R. 3158 was made at the Fall Meeting of the Maritime Law Association on November 1, 1985.

On April 30, 1986, the Finance Committee held its Spring Meeting at which I was authorized to communicate the enclosed comments to you.

The comments set forth on the chart include references to the following provisions of H.R. 3158 which could involve substantive changes of serious concern to the Finance Committee:

Subsection 31301(3):

The definition of "necessaries" has given rise to much litigation. The Current Statute does not purport to define "necessaries", but creates a lien in favor of "any person furnishing repairs, supplies, tonnage, use of dry dock or marine railway, or other necessaries". H.R. 3158 purports to give a partial definition of "necessaries" without affording a clear signal that a comprehensive definition is a matter of case law.

Subsection 31301(5):

The Current Statute (46 U.S.C. §951) provides that the definition of "preferred mortgage" includes a "mortgage, hypothecation or similar charge"* that has been "duly and validly" executed and "duly" registered. H.R. 3158 only requires that the "mortgage" be "executed" and "registered" to constitute a preferred mortgage. Thus, under H.R. 3158 a mortgage that is purportedly executed and registered pursuant to the laws of the country under which the vessel is documented will constitute a preferred mortgage even though the mortgage may not have been "duly and validly" executed and "duly registered" in accordance with such laws.

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*Subdivision (B) of H.R. 3158 initially discusses mortgages, hypothecations and similar charges, but then limits its discussion to mortgages only.

Subdivision (B) of H.R. 3158 refers to "a mortgage, hypothecation, or similar charge that is security on a documented foreign vessel", whereas the Current Statute (46 U.S.C. §951) refers to any "mortgage, hypothecation, or similar charge created as a security upon any documented vessel". This change may be substantive since under the Current Statute a mortgage, hypothecation or similar charge that does not give rise to a maritime lien under the law of its flag can be enforced as a preferred mortgage lien in the United States.

Section 31302:

H.R. 3158 does not include the requirement set forth in the Current Statute (46 U.S.C. §927) that, upon request, the collector of customs furnish a certificate setting forth the names of the owners of a vessel, the interest held by each owner and material facts relating to the bill of sale, mortgage, lien or encumbrance covering a vessel. Without this provision, a party does not have any right to obtain such a certificate.

Section 31321:

Subdivision (a)(3) of H.R. 3158 requires that a third party have actual knowledge of an unrecorded instrument for the instrument to be valid against such third party. This creates a substantive change from the Current Statute (46 U.S.C. §921(a)), which imposes a less stringent requirement than that provided for in H.R. 3158, in that it can be read to require that the third party have actual notice of (a) the transaction involving the instrument or (b) the instrument itself.

Section 31322:

Section 926(c) of the Current Statute (46 U.S.C. §926(c)) has not been included in H.R. 3158. Thus, there is no provision governing the recording of bills of sale, conveyances and mortgages in the case of a change in the port of documentation of a United States vessel.

Section 31329:

H.R. 3158 requires approval of the trustee whenever an evidence of indebtedness secured by a mortgage to a trustee is issued, assigned, or transferred to a person not a citizen of the United States. This differs substantively from the Current Statute (46 U.S.C. §961(e)) which provides that an evidence of indebtedness can be issued, transferred or assigned to a person who is not a United States citizen, provided such action is approved by the Secretary of Transportation, even if the trustee has not been approved by the Secretary.

In addition, subsection (c) of H.R. 3158 retains the reference to a single right under a mortgage, whereas the Current Statute (46 U.S.C. §961(d)) refers to "rights" under a mortgage.

A major substantive change resulting from the revision of subsection (d) of H.R. 3158 is that this provision permits the sale of a vessel to a non-United States citizen by order of a district court with the approval of the Secretary, whereas the Current Statute (46 U.S.C. §961(f)) prohibits such sale to a non-citizen without exception.

Section 31342:

In setting forth the criteria for the establishment of maritime liens, H.R. 3158 refers to a person "providing" necessaries, whereas the Current Statute (46 U.S.C. §971) refers to a person "furnishing" necessaries. There is no apparent reason for this change. On the other hand, subsection 31326(b)(2) of H.R. 3158, relating to those liens entitled to priority over a preferred mortgage, retains the language of the Current Statute (46 U.S.C. §951) in referring to necessaries "performed or supplied", thereby alleviating any doubt that the issue of territory, i.e. where the necessaries are performed or supplied, is still determinative. The substitution of "providing" for "furnishing" in Section 31342 of H.R. 3158 may raise an issue as to whether the concept of territory is now to be read into the question of whether or not a maritime lien has been created. As stated previously, since the issue of necessaries is a subject of much litigation, the Finance Committee requests that Section 31342 retain the word "furnishing" as used in the Current Statute.

In addition to the comments set forth above, there are certain provisions of the Current Statute, retained in H.R. 3158, that the Finance Committee recommends be deleted from the statute, even though such deletions would constitute substantive changes. These provisions include the requirements that in order to constitute a preferred mortgage: (a) the mortgage be endorsed upon the documents of a vessel (§31322(a)(4) and (d) of H.R. 3158; 46 U.S.C. §922(a)(1) and (c) of the Current Statute); (b) the mortgage be accompanied by an affidavit of good faith (§31322(a)(5) of H.R. 3158; 46 U.S.C. §922(a)(3) of the Current Statute); and (c) the mortgage not stipulate that the mortgagee waives the preferred status (§31322(a)(6) of H.R. 3158; 46 U.S.C. §922(a)(4) of the Current Statute). The consensus of the Finance Committee is that these requirements serve no useful purpose.

Please feel free to contact me should you wish to discuss any of these comments in further detail and kindly keep me informed as to the scheduling of any Congressional hearings in respect to H.R. 3158.

Sincerely,

Amy Siegel

AS:cf
Enc.

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BRUCE A. KING

July 19, 1988

FEDERAL EXPRESS

Mr. John Cullather
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Washington, D. C. 20515

Re: American Bar Association - Ship Financing Act

Dear John:

Thank you for sending me your recent draft of HR 3105. I have reviewed this and the MLA's suggested revisions of July 18. I am in general agreement with the MLA's suggestions. Beyond what the MLA has proposed, I have made some suggestions. For simplicity, I have marked my suggestions on the enclosed copy of the MLA's draft, since some of my language has an effect on both the MLA's draft and the staff's revision of HR 3105. Many of my suggestions are self-explanatory. For those that aren't, I refer to them below by section number:

§31301(6)(B) I recall from our June 29 meeting that Emery Harper suggested clarifying that the foreign mortgages under this provision need to be recorded where the ownership of the foreign vessel is documented, since a demise charterer of a foreign vessel can often simultaneously register the vessel and charter in another country. Mr. Harper also suggested contacting Capt. Frederick Rosa at the Coast Guard to approve the actual language used, if the suggestion is adopted, since he has done a great deal of work in this area.

§31304(a)(1) One of the principal ABA objectives has been to relieve the Coast Guard of its perceived responsibility to make a determination at the time of recording whether a mortgage is in fact a preferred mortgage. In practice this means that Coast Guard personnel often actually read these documents cover to cover, which adds to the time it takes to process documents. We'll all be helped if the Coast Guard can simply look for the statements required in §31321 and process the document. Tom Willis made very clear that it is the liability provisions of the Act which engenders their caution, so I have suggested some relief. After all, if a shipowner is willing to sign a deficient mortgage and a bank is willing to accept it, who but they should care?

§31306(5) The reference to "documented" should be deleted here, because the priority of a preferred mortgage is tied to the time of the filing of the mortgage, which can precede actual documentation.

§31321 and §31322 These sections still do not clearly permit a mortgage to be signed on a day prior to the day when an application for a document or the mortgage itself is filed. This is central to reducing the cost and inconvenience in complying with the Act. I have suggested language to clarify this. Also, it would be very useful if the Coast Guard could be required to record mortgage subordination agreements. This would make it possible for a mortgagee to subordinate his mortgage to another mortgagee without having to ask the Coast Guard to re-record a mortgage.

§31321(b)(2) The suggestion to change "the addresses" to "an address" is to ensure that a mortgage does not fail because someone failed to correctly pick the most appropriate address for a party with several plausible addresses.

§31321(b)(3) The addition of "miscellaneous charges" is important in this context. There are many miscellaneous charges that almost all mortgages cover (such as a mortgagee's advances of insurance premiums if the shipowner fails to insure the vessel) that are not "interest", "costs" (which would be judicially construed as court costs), or "fees" (which would be construed to mean litigation attorneys' fees). Miscellaneous charges is a better, and is a more inclusive term for accomplishing the same objective.

§31321(c)(2) Because the priority of a mortgage will be fixed as of the time of filing, it is very important that the Coast Guard maintains records of the exact times of filing. I would suggest being specific on this point, because it is so essential to priority determination.

§31322(a)(1)(c)(iv) As drafted this catchall may inadvertently omit mortgage trustees approved under 46 U.S.C. §§808 and 835 and §31329.

§31322(a)(2) 46 U.S.C. §951 opens by stating that a preferred mortgage shall constitute a lien. This is a valuable statutory statement, and this is an appropriate place for it.

§31322(b) As a matter of contemporary loan terminology, the debt bears interest, not the mortgage. Also, 46 U.S.C. §925(d) refers to "bearing" interest rather than "having" it.

§31329(a) The phrase I suggest inserting is necessary to ensure that the existing practice of having the mortgage trustee also hold the promissory note in trust for foreign lenders be permitted to continue.

§31329(C) Distinguishing "legal" from "beneficial" rights would clarify that the beneficiary of a mortgage trust may transfer the beneficial interest to another foreign lender (i.e. assign the loan) so long as a U.S. trustee is mantained.

§31341(a) I have just noticed a major change here to existing law. Under 46 U.S.C. §972, a specified list of officers and agents are rebuttably presumed to have authority from the owner to procure necessaries for a vessel. Under 46 U.S.C. §973, to the extent those same officers and agents are appointed by charterers, owners pro hac vice, or by agreed purchasers in possession of a vessel, those same individuals are still presumed to have authority to procure necessaries. When read together with §972, it is clear that §973 does not generally impower charterers, owners pro hac vice, or agreed purchasers in possession to incur maritime liens unless the owner has placed them in a position to appoint the officers and agents described in §972. Section 31341(a) of HR 3105 would give them this general authority to incur liens on a vessel, and greatly diminishes the control which an owner has over people he deals with with regard to protecting himself against maritime liens. I have suggested a modification to conform to existing law.

§31344 In the event the MLA's suggestion for incorporating §31344 into §31326 is not adopted, I would like to point out that at §31344(b)(2) the reference to "necessaries performed or supplied for the vessel" should be changed to refer to providing or furnishing necessaries to the vessel in accordance with the final language that is selected for §31301(4).

If you have any questions concerning my suggestions, please do not hesitate to give me a call. I'd be happy to discuss them at any time.

Very truly yours,

BOGLE & GATES

Bruce A. King

cc: Mr. David McI. Williams
James Kemp, Jr.

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July 22, 1988

FEDERAL EXPRESS

The Honorable Walter B. Jones
Chairman
Committee on Merchant Marine
  and Fisheries
1334 Longworth
U.S. House of Representative
Washington, D.C. 20515-3301

Re: H.R. 3105 - Proposed Recodification of
Title 46 U.S. Code dealing with Ship
Mortgages and Maritime Liens

Dear Mr. Jones:

The Marine Finance Committee (the "Finance Committee") of the United States Maritime Law Association has reviewed the Draft Changes to H.R. 3105 (the "House Draft") and notes, with gratitude, the incorporation therein of a large number of the suggestions and recommendations previously made on behalf of the Finance Committee.

In response to certain of the changes set forth in the House Draft, the Finance Committee has proposed limited further revisions to H.R. 3105. These revisions are set forth in the mark-up of H.R. 3105 (the "MLA Draft") provided to you by David McI. Williams, Esq. of Semmes, Bowen & Semmes, and are marked to show changes from the House Draft, as follows: shaded text denotes additional language suggested by the Finance Committee and bracketed text denotes language which the Finance Committee suggests be deleted.

The purposes of this letter are twofold: (i) to provide explanation for the changes suggested by the Finance Committee (please note that many of the changes in the MLA Draft are self-explanatory and, as such, no further explanation is provided herein), and (ii) to assist in formulating a legislative history that will provide guidance to the maritime community in the years to come.

The major changes suggested by the Finance Committee fall within several broad categories which are summarized, as follows:

1. Provisions Relating to "Necessaries"

The determination of those parties entitled to a maritime lien for "furnishing ... necessaries to [a] vessel" has been the subject of extensive litigation. As a result, there now exists a body of case law construing those provisions of Title 46 of the United States Code as presently in effect (the "Current Statute"). In particular, the use of the verb "to furnish" in the Current Statute has been closely examined by the courts, see e.g., Foss Launch & Tug Co. v. Char Ching Shipping U.S.A., 808 F.2d 697 (9th Cir. 1987), cert. denied, Itel Containers International Corp. v. M/V San Francisco, 108 S.Ct. 96 (1987) and the cases cited therein.

The Finance Committee is deeply concerned that any change in the above-mentioned language, even though such a change may presently appear to be immaterial, may provide grounds for a determination that a substantive change in the law was intended as a result thereof. For this reason, the Finance Committee proposes that the word "provided" be replaced by the word "furnished" in §§31305 and 31342 of the House Draft.

Similarly, recently decided cases (see e.g., Mobil Sales & Supply Corp. v. Panamax Venus, 804 F.2d 541 (9th Cir. 1986); Morgan Guaranty Trust Company of New York v. M/V Grigorios C. IV, 615 F.Supp 1444 (E.D. La 1985)) have settled the law in respect of the construction of the phrase "performed or supplied in the United States" [See 46 U.S.C. §951 of the Current Statute]. For the same reasons as set forth above, it is strongly recommended that §31326(b)(2) of the House Draft be revised so as to retain this language, without amendment.

The Finance Committee recommends that the words "but is not limited to" be inserted after the words "necessaries includes" in §31301(4). The word "includes" standing alone is ambiguous in that it may be interpreted in a restrictive sense without the addition of the proposed phrase. This concern has been expressed to members of the Finance Committee by a number of representatives of marine suppliers. At the very least the Finance Committee recommends, in view of the sensitivity in the marine community to this issue, that the legislative history and the report make it clear that the word "includes" as it is used specifically in this section means "includes but is not limited to."

2. Permitting Instruments to be Filed for Recording

The Current Statute requires that a vessel be documented before it can be the subject of a preferred mortgage. As has been pointed out in previous testimony in respect of H.R. 3105, there are presently severe backlogs in the processing by the Coast Guard of applications for documentation in respect of non-commercial vessels, resulting in lenders being deprived of the benefits of a preferred ship mortgage, and possibly being rendered unsecured, for a period of several months after the making of a loan. This backlog extends beyond applications for documentation to instruments submitted to the Coast Guard for recording. The problems that such a backlog can cause were recently demonstrated in In Re Alberto, 823 F.2d 712 (3d Cir. 1987), which involved a shipowner who filed a petition for relief under the United States bankruptcy laws between the time a mortgage was presented for recording and the time the actual recording took place. The trustee-in-bankruptcy argued that the mortgage was not perfected prior to the filing of the bankruptcy petition. The Third Circuit construed the provisions of the Ship Mortgage Act to provide that the mortgage recording would be effective from the time of the filing of the mortgage with the Coast Guard provided that the files of the Coast Guard were available for public inspection and were maintained in a manner that would put a third party on notice of the existence of the mortgage.

The Finance Committee has explored numerous solutions to the backlog problem, which has most directly impacted the financing of pleasure vessels, and recommends an approach that would permit the filing for recording of bills of sale, conveyances, mortgages, and assignments, assumptions, amendments and supplements to a mortgage (collectively, "Vessel Instruments") relating to a vessel which is documented or in respect of which an application for documentation is filed. The issue of timing as it relates to the determination of priorities, would be keyed to the time the Vessel Instrument is filed for recording.

The main features of the system envisioned by the Finance Committee* are as follows:

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*The MLA Draft contains two (2) versions of §31321. The version which most closely adheres to the House Draft is hereinafter referred to as the "MLA Principal Draft." A second proposal has been submitted separately from the balance of the MLA Draft and is hereinafter referred to as the "MLA Alternative Draft".

(i) A Vessel Instrument may include any part of a documented vessel or a vessel for which an application for documentation is filed (see §31321(a)(1) MLA Principal and Alternative Drafts). Thus, the concept of application for documentation will be applicable throughout H.R. 3105 wherever the House Draft contemplates the recording of a Vessel Instrument in respect of a documented vessel. It is envisioned that a documented vessel would be identified (e.g., by its name and official number) and that a vessel for which an application for documentation has been filed would be identified by a hull number or some other identifying characteristic that would enable the Coast Guard to promptly index the application and any Vessel Instrument filed in respect of the vessel in order to afford third parties a means of determining the existence thereof. Implied in this scheme is the notion that a preferred ship mortgage can be made before the subject vessel is documented or an application for documentation in respect thereof is filed.

The regulations in respect of this provision would have to provide a method of determining the proper place for filing applications for documentation and Vessel Instruments and of protecting against a shipowner filing an application for documentation for a single vessel in more than one location.

(ii) Prior to its recordation, a Vessel Instrument may be "filed for recording" with the Secretary of Transportation (the "Secretary") (see §§31302, 31321(a)(1) MLA Principal and Alternative Drafts). Thus, the concept of "filed for recording" will be applicable throughout H.R. 3105 wherever the concept of recording such an instrument currently appears. The Vessel Instrument will, from the time of its filing for recording, be valid and effective as against third parties (see §31321(a)(2) MLA Principal and Alternative Drafts). Thus, it will be necessary for the Coast Guard to devise a system of clocking-in Vessel Instruments so as to avoid any dispute as to priority resulting from the time of filing for recording.

(iii) Vessel Instruments will be recorded by the Secretary, upon the documentation of the vessel, in the order in which they are (A) received for filing (see §31321(c) MLA Principal Draft), or (B) filed for recording (see §31321(c) MLA Alternative Draft).

(iv) The notion of substantial compliance, which is implied under the Current Statute, has been expressly set forth in the MLA Alternative Draft (see §31321(e) MLA Principal Draft and §31321(b)(2) MLA Alternative Draft). Although this suggestion does not create a change from the law as it is presently construed, it is important that this concept be expressly stated inasmuch as applications for documentation and Vessel Instruments may not be reviewed by the Coast Guard when they are submitted for filing. Such a review may not occur until the vessel is ready to be documented and the Vessel Instrument is able to be recorded which may be several months from the time that the application and/or Vessel Instruments are filed. It should be the intent of the statute that an application not be rejected nor a Vessel Instrument lose its priority as the result of a technical omission or deficiency.

(v) In order for this system, which envisions a prompt indexing (see §31321(c)(2) MLA Principal and Alternative Drafts) of a Vessel Instrument upon its filing for recordation, to be successful, the current role of the Coast Guard, effectively imposed by the present statutory scheme, in reviewing the substantive provisions of a Vessel Instrument would be substantially reduced. Rather, initial Coast Guard review would focus on the limited criteria (see e.g., §31321(b) MLA Principal and Alternative Drafts) set forth in the applicable statutory provision.

(vi) In the event that the Secretary determines that a vessel, in respect of which a Vessel Instrument has been filed for recording, cannot be documented, the Secretary should give sufficient notice of such determination to the interested parties before terminating the filing and returning the instrument (see §31321(e) MLA Alternative Draft). The Finance Committee recommends that the regulations provide specific instructions as to, inter alia, the parties to whom the Secretary should return the applications and Vessel Instruments.

3. International Recognition of Mortgages and Hypotheques

Although the United States is not a party to any International Convention relating to rules on maritime liens and mortgages** any recodification of the provisions of the U.S. Code dealing with ship mortgages and maritime liens should be mindful of these International Conventions since many of the provisions thereof have been adopted as domestic law by foreign jurisdictions and compliance with such provisions will assist in obtaining recognition of United States ship mortgages in those jurisdictions.

Several provisions of the House Draft must be viewed in light of these International Conventions. The House Draft (§31301(6)(B)) provides that a "preferred mortgage" means a mortgage, hypothecation, or similar charge that is "established" as a security on a documented foreign vessel ... The Finance Committee recommends that the term "established" be replaced by the term "effected" which is the term employed in the 1926 Convention, the 1967 Convention and the 1985 Draft. To use a different term affords an opportunity for a foreign court to determine that a mortgage "established" as a security meets a lesser standard than a mortgage "effected" as a security and that such mortgage is not entitled to the international recognition afforded by the International Conventions.

Section 31301(6)(B) of the House Draft also requires that the mortgage be executed under the laws of the foreign country under whose laws the vessel is "documented." The use of the word "documented" may create uncertainty in a situation involving a vessel the ownership of which is registered under the laws of one country (e.g., Liberia), but which is temporarily permitted to fly the flag of another country (e.g., Philippines) under a bareboat charter registry scheme. Under a technical interpretation of this scenario, the vessel may be deemed to be "registered" under the laws of Liberia but temporarily "documented"

**There are two proposed International Conventions on the subject:

(a) International Convention for the Unification of Certain Rules Relating to Maritime Liens and Mortgages, Brussels, 1926 (the "1926 Convention"); and

(b) International Convention for the Unification of Certain Rules Relating to Maritime Liens and Mortgages, Brussels, 1967 (the "1967 Convention").

The 1926 Convention has received approval in over 20 countries; the 1967 Convention, in about half a dozen. In 1985 a CMI Conference in Lisbon produced a Draft Revision of the 1967 Convention (the "1985 Draft"). An intergovernmental group is currently reviewing the provisions of these International Conventions under the joint auspices of IMO and UNCTAD (the "Joint Group").

under the laws of the Philippines. Even though a mortgage against the vessel would always be made and recorded under Liberian law, there might be a question as to whether such a mortgage would constitute a preferred mortgage under §31301(6)(B) of the House Draft if it were not also registered in some fashion in the Philippines, the argument being that the vessel is also, in a broad sense, "registered" in that country. We believe the sound interpretation is that registration of the mortgage in Liberia only, the underlying vessel registry notwithstanding the temporary use of the Philippines flag, is mandated by the present statute. We note that the International Conventions present a similar interpretive issue and we understand that a clear consensus has emerged in the Joint Group studying maritime liens and mortgages that registration of the vessel mortgage in the country of bareboat charter registry should not be required for international recognition and that any future convention covering the subject should make that clear. The Joint Group has also apparently reached the conclusion that the existing conventions should be interpreted in a manner consistent with this view, i.e., that the place of mortgage registration is the country of the underlying, or permanent, registration of the vessel."

Under the 1967 Convention and the 1985 Draft, the register in which instruments are registered, and the instruments required to be registered must be open to public inspection and extracts of the register and copies of the registered documents must be available. Under the 1926 Convention instruments must be registered in a public register.

The foregoing language stresses the importance under the International Conventions of an open, public registry in order to qualify for international recognition of a Vessel Instrument. The Finance Committee believes that the revisions set forth in §§31302(b) and 31321(c)(2) of the MLA Principal and Alternative Drafts help to achieve this goal.

4. Vessel Instruments and Requirements thereof

The Finance Committee has added to the list of instruments which may be recorded or filed for recording, assumptions, amendments and supplements to mortgages (see §31321(a)(1) MLA Principal and Alternative Drafts). This notion is carried through the MLA Draft wherever the concept of Vessel Instruments appears.

The Finance Committee questions, however, whether a subordination agreement, which is a private agreement generally between two or more creditors, should be the subject of a public filing and/or recording.

Under the system proposed in the MLA Draft, the legislative intent underlying §31321(b) will be of extreme importance in helping the Coast Guard to reduce the time required by it in reviewing Vessel Instruments which are submitted for filing.

The Finance Committee has therefore proposed the following revisions:

(a) §31321(b)(1) (Principal Draft), §31321(b)(1)(A) (Alternative Draft) - Since more than one vessel may have the same name, a vessel should be identified by some other characteristic, for example, official number, to be more particularly set forth in regulations.

(b) §31321(b)(3) (Principal Draft), §31321(b)(1)(C) (Alternative Draft) - Amount of the Mortgage - the House Draft has come a long way in recognizing the large variety of modern financing transactions which may be secured by preferred ship mortgages. However, the MLA Draft sets forth a few additional revisions to this provision:

(i) The Finance Committee suggests that the word "maximum" be deleted since such language could be construed in foreign jurisdictions as imposing a ceiling on the amount recoverable by the mortgagee. For this same reason the MLA Draft clarifies that the amount stated is exclusive of interest, expenses and fees. The Finance Committee is not in favor of use of the word "principal" amount which could be viewed as limiting the type of transaction;

(ii) The Finance Committee also recommends that the phrase "for which the mortgagor is liable" be deleted inasmuch as it may not appear to allow for non-recourse mortgages. Non-recourse mortgages are contemplated by Section 1104(b)(7) of Title XI of the Merchant Marine Act of 1936 and also are fairly common in private commercial transactions.

(iii) The addition of the language "direct or contingent" confirms that mortgages may secure contingent obligations;

(iv) The Finance Committee believes that it will be of enormous assistance if the legislative history and/or regulations in respect of this provision (A) clarify that the amount of the mortgage refers to the amount at any one time outstanding such that, in connection with revolving credit transactions, the amount need not include all possible advances that may be made (and repaid) throughout the course of a transaction, and (B) confirm that the term "unit of account", which has become a recognized concept under the maritime laws of certain foreign jurisdictions, should be construed as broadly as possible so as to allow for a myriad of alternate currency transactions as well as financing arrangements which may be developed in the future.

(c) §31321(b)(4) and (6) of the House Draft - The Finance Committee also suggests that the requirements that the Vessel Instrument state the interests of the grantor, mortgagor, or assignor in the vessel and the date of maturity be deleted inasmuch as the requirement of an endorsement has been omitted and such data is not required under the International Conventions.

5. Rate of Interest

The Finance Committee requests that the legislative history in respect of §31322(b) of the MLA Draft reflect that this provision is intended to reaffirm the long-standing practice of treating the section as covering all kinds of rates and formulae for the calculation of interest, finance charges and time-price differentials, however designated in any obligation secured by a preferred mortgage. It is intended, and accepted current practice, that such rates may be fixed, variable or convertible so long as the actual rate or formula for arriving at a variable or convertible rate is set forth in such obligation. It is further intended that the rate or formula for arriving at it need not be set forth in the mortgage so long as it is specified in the obligation and the obligation is clearly identified in the mortgage. Moreover, such legislative history should provide that it is intended that where the obligation is executed contemporaneously with or prior to the mortgage and the obligation requires the mortgage as security, this section shall apply from the date of the obligation so that there is no gap between the date interest begins to accrue and the date of the filing of the mortgage.

Assuming that the legislative history reflects the foregoing, the Finance Committee recommends against revision of the wording of the House Draft in this regard.

In addition to the foregoing general categories, there are a number of additional revisions suggested by the Finance Committee which warrant brief explanation:

(a) §31301(1)(A) - The Finance Committee suggests that the word "jurat" be deleted from the definition of "acknowledge" inasmuch as a "jurat" is defined as a "certificate of officer or person before whom writing was sworn to "(Black's Law Dictionary, 4th Ed.). Vessel Instruments are generally not sworn to, nor does the Current Statute require that this be done. Rather, the Current Statute requires that Vessel Instruments be acknowledged which is defined by Black's as a "formal declaration before authorized official, by person who executed instrument, that it is his free act and deed." The same concept should appear in the recodification.

(b) §31301(3)(B) - The addition of the phrase "for holders of indebtedness" parallels the language of §31329 of the House Draft. The additional revisions made by the Finance Committee modernize and broaden the definition of "mortgagee" wherein the underlying transaction involves a trust relationship. The Current Statute limits a trust relationship to one involving a trust deed and a bond issue under the deed and does not take into account other financing arrangements involving a trust.

(c) §31301(5) - The addition of the term "maritime" clarifies that the term "preferred maritime lien" only refers to "maritime" liens.

(d) §31302(d) - The Finance Committee has deleted this provision of the House Draft and added it to §31321(b)(5) of the MLA Principal Draft and §31321(b)(1)(E) of the MLA Alternative Draft.

(e) §31309 - The Finance Committee believes that the Secretary needs broad authority to prescribe regulations necessary to carry out the statutory scheme and should not be confined to the limited list set forth in the House Draft.

(f) §31322(b) and (d) - The Finance Committee recommends that these provisions of the House Draft be deleted and replaced by a single new subsection (c) which treats property other than a vessel in the same manner in which the House Draft treats preferred mortgages including more than one vessel. As such, a mortgage will not lose its preferred status simply because it includes property other than a vessel but fails to provide for the separate discharge of such property.

(g) §31325 - The modifications to §31325(b) suggested in the MLA Draft clarify that a mortgagee may bring an in personam action in admiralty against the mortgagor and any guarantor, co-maker, surety, or any other person obligated to pay all or any part or any deficiency in respect of the outstanding indebtedness secured by the mortgage, and confirm that such actions can be litigated in a single forum.

The proposed language of §31325(c) of the House Draft could be viewed as changing the law so that preferred mortgages could only be enforced in American courts. Under existing law, preferred mortgages may be enforced by foreign courts if the vessel covered by the mortgage is located within the jurisdiction of the foreign court. The Finance Committee therefore proposes that this provision remain as it is under the Current Statute.

The legislative history in respect of §31325 should also reflect (a) that the lien of a preferred mortgage may be enforced in any foreign country in which the vessel may be found pursuant to the procedure of said country for the enforcement of mortgages or similar obligations on vessels, and (b) that nothing in this section is to be construed as intending that a party who exercises any rights it may have under state law, waives its right to a deficiency judgment under this section.

The additional language suggested by the Finance Committee in §31325(d) renders the provision applicable to actions to enforce a maritime lien as well as to actions to enforce a preferred mortgage and requires that notice of such a civil action be given to a mortgagee of record. We believe there is a broad concensus in the maritime finance community that such a requirement of notice should be provided for and that the MLA Draft effectively conforms the statute to current practice.

(h) §31329(a)(3) - Since §31329(a)(1) requires that the trustee be a corporation, the inclusion of the language "an individual who is a national of the United States" was inappropriate. The Finance Committee believes that these changes reflect the intent of the House Draft.

(i) §31329(d)(1)(B) - The additional language in the MLA Draft distinguishes this paragraph from §31329(d)(1)(C).

(j) §31341(a) - The Finance Committee believes that the legislative history of this provisions should confirm that the House Draft is not intended to and should not be deemed to constitute a substantive change from the current law regarding persons authorized to incur liens on vessels.

(k) §31343(c) - As in the case of a preferred mortgage, the provision of a discharge should only be required upon the discharge, in full, of the indebtedness.

(l) §31344 - This section has been deleted inasmuch as it is now included in Section 31326.

Please note that in reviewing the House Draft, and particularly the definitions set forth in §30101, the Finance Committee has only focused upon the definitions of terms appearing in or relating to Chapter 313 - Commercial Instruments and Maritime Liens. Those definitions which are applicable to provisions elsewhere in Title 46, United States Code were felt to be outside the expertise of the members of the Finance Committee as a whole. As such, we have intentionally refrained from commenting upon those definitions.

The Finance Committee strongly requests that the legislative history address the treatment to be afforded (a) those Vessel Instruments that will be on file with the Coast Guard, but not yet recorded, at the time that the recodification becomes effective; and (b) Vessel Instruments which have been recorded, but which contain some technical defect, which would not be a defect under the recodification (e.g., defective endorsement). The Finance Committee suggests that Vessel Instruments already recorded or presently awaiting recordation should derive the benefits of the recodification provided they are in substantial compliance with the Current Statute.

Please feel free to contact me if the Finance Committee can be of any further assistance in respect of the foregoing.

Very truly yours,

Richard B. Teiman

ABS:RBT/hty

cc: Mr. John M. Cullather
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Richard B. Barnett, Esq.

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September 2, 1988

The Honorable Walter B. Jones
Chairman
Committee on Merchant Marine and Fisheries
133 Longworth House Office Building
U. S. House of Representatives
Washington, D. C. 20515-3301

Re: HR 3105 - Proposed Recodification Title 46
U.S. Code dealing with Ship Mortgages
and Maritime liens

Dear Mr. Jones:

On behalf of the Subcommittee on Maritime Financing of the American Bar Association, I write to state that we concur with the comments on HR 3105 submitted to you on September 2, 1988 by the Committee on Marine Finance of the Maritime Law Association of the United States (the "MLA"). We have worked closely with the MLA in formulating these proposals and are of the view that their implementation would avoid much needless controversy in the future.

We understand that in the current draft of HR 3105, 46 U.S.C. §31329 reads as enclosed. It is this version with which we concur, and we concur. It would appear that in this version of §31329, in substance subsection (d) already covers the MLA's suggested addition to §31329(d). In any event, §31328(e) and §31329(d) ought to be consistent.

Paragraphs 2 and 3 of the MLA letter are of particular importance. The suggestions in paragraph 2 will avoid traps for the unwary in applying the statute. The proposal in paragraph 3 will also avoid the suggestion that an instrument presented for filing that is not in compliance with the Act is unlawful as opposed to simply being ineffective, which is all that we should be concerned about.

We have a couple of additional minor suggestions for clarity:

1. In the markup version of HR 3105 submitted by the MLA, on the top line of page 8 we believe the words "of the lien" were omitted from the suggested insertion of "the priority."

2. In §31325(b)(2) and (3), "comaker" and "guarantor" should be plural, so that it is clear that actions may be brought against any or all comakers or guarantors.

3. In §31325(d)(1) the phrase "to enforce a maritime lien" should read "to enforce another maritime lien." OK

4. The date in the MLA insertion to §106(b) should probably read December 31, 1988.

I concur with the MLA's concern over the lack of time necessary to enable the maritime industry to effectively analyze the current proposals regarding the formation of a vessel identification system and altering the legal status of security interests perfected under state law. The ABA subcommittee has not been able to consider these proposals.

We appreciate your interest in reform to the Ship Mortgage Act. If I can be of any assistance, or if you have any questions concerning our suggestions, please do not hesitate to contact me.

Very truly yours,

Bruce A. King
Vice Chairman
Subcommittee on Maritime Financing
American Bar Association

cc: Mr. James B. Kemp, Jr.
Mr. Richard Barnett
Ms. Amy Siegel
Mr. David McI. Williams

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Richard B. Barnett
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September 2, 1988

The Honorable Walter B. Jones
Chairman
Committee on Merchant Marine and Fisheries
133 Longworth House Office Building
U.S. House of Representatives
Washington, D.C. 20515-3301

Re: H.R. 3105 - Proposed Recodification
Title 46 U.S. Code dealing with
Ship Mortgages and Maritime Liens

Dear Mr. Jones:

The Committee on Marine Finance (the "Finance Committee") of the Maritime Law Association of the United States has reviewed the draft of H.R. 3105 (the "Committee Draft") reported out of the Committee on Merchant Marine and Fisheries on August 4, 1988. Many of the recommendations previously made on behalf of the Finance Committee, including those set out in Richard Teiman's letter of July 22, 1988, have been incorporated in the Committee Draft. The Finance Committee is very grateful for your attention in these regards.

After consideration of the Committee Draft, the purpose of this letter is to set forth a limited number of further revisions to the legislation recommended by the Finance Committee. The specific text of these recommendations is set forth in the attached "markup" of the bill as follows: underlined text denotes additional language and bracketed text denotes language to be deleted. Several of our recommended changes are self-explanatory. This letter is to provide you an explanation of certain of our recommendations and some considerations for inclusion in the legislative history for the bill.

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Our recommendations are as follows:

1. Section 31301(3)(B). We suggest elimination of the words "authorized under section 31328 of the title". A trustee may be used to hold a mortgage on a vessel for reasons wholly unrelated to non-citizenship of a lender. For example, a trustee may be used for administrative convenience where there is a large group of lenders even if all of the lenders are citizens.

2. Section 31321(a)(1). We suggest that the language "whenever made" be moved from section 31322(a)(1) to section 31321(a)(1) and that language "that is in substantial compliance with the requirement of Chapter 121 of this title and the regulations prescribed under that chapter" be moved from section 31322(a)(a)(C)(ii) to section 31321(a)(1). We believe these changes will clarify that all mortgages, not merely preferred mortgages, can be executed and delivered prior to the documentation of the vessel and that the substantial compliance doctrine applies to bills of sale, conveyances, etc. as well as to mortgages. We suggest that the legislative history indicate what "related instrument" includes such as amendment, assignment, assumption and supplement.

3. Section 31321(a)(3). We recommend this provision be deleted entirely. The language of this subsection in its current form could well be construed to create unintended rights in persons not parties to financing transactions, with unexpected and incongruous results. The purpose of this section to redefine the role of Coast Guard documentation personnel examining instruments will be performed by the addition of the new subsection 31321(e)(2).

4. Section 31321(e). This language indicates that the obligation of the Coast Guard is limited to a ministerial examination of documents to verify substantial compliance with the statutory requirements.

5. Section 31322(a)(1)(C)(ii). If our suggestion in paragraph 2 above is not accepted, the terms "has been filed" on lines 2 and 3 of page 7 should be replaced with "is filed," in conformity with the provisions of section

31321(a)(1) at line 26 on page 7. The purpose is to make clear that a mortgage may attain preferred status notwithstanding that it may have been signed, sealed, and delivered (and therefore "made") at a loan closing occurring before the application for documentation of the vessel has been filed.

6. Section 31322(a)(3). Between lines 18 and 19, insert new subsection (3) to make clear that a mortgage entitled to preferred status attains that preferred status at the time of filing in compliance with the requirements of subsection (a). While this is the implicit result of the text presented in the Committee Draft, our Finance Committee believes that this aspect should be made explicit in the statute. An additional reason to exclude the word "documented" is that our courts are also called upon to foreclose liens on undocumented vessels both U.S. owned and foreign. The word is inconsistent with section 31326(b)(2).

7. Section 31322(c)(2). Our proposal for change to this subsection is intended to remove an outdated and impractical formula. The current text should be replaced with provisions making clear that the outstanding amount of the mortgage indebtedness is not discharged until satisfied. The confirmed sale of a vessel in rem should always result in the discharge of all liens, but in accordance with widely accepted modern financing principles, the mortgage indebtedness should only be discharged to the extent of the proceeds of sale. In the case of a fleet mortgage, or a mortgage covering non-vessel property, the mortgagee's recourse to these other vessels or property should not be limited except to prevent more than one satisfaction of the entire debt.

8. Section 31325(b). We recommend no change to the text, but point out the critical importance of the permissive verb "may enforce" at line 24. A mortgage foreclosure action is seldom the mortgagee's sole remedy under the mortgage instrument and nothing in the Ship Mortgage Act is intended to preclude avail to other remedies. Repossession and resale of mortgaged vessels under state law (Uniform Commercial Code) authorities has been a common practice in the yacht financing history. The decision of one district court in Bank of America Nat'l Trust

Savings Ass'n v. Fogle, 1986 AMC 2005 (D. Ore. 1985), holding that the Ship Mortgage Act preempts alternative state law remedies, should be expressly disapproved in the legislative history to this section.

9. Section 31326(a). We urge that the word "documented" be deleted from the text for this section, at line 29 on page 9. Under the provisions of sections 31321 and 31322, a mortgage may attain preferred status upon filing, before the completion of documentation of the vessel. Having attained preferred status, the mortgage is subject to foreclosure under section 31325. The principles set forth in 31326(a) should apply to the *in rem* sale of any vessel subject to a preferred mortgage or a maritime lien, regardless of whether the vessel is documented.

10. Section 31326(b)(2). We strongly recommend that the legislative history make clear that the substitution of the word "provided" for "performed or supplied" is not intended to change existing law.

11. Section 31328(a). We recommend the insertion of language to make clear that the transfer of a note to *any* non-citizen is prohibited without the approval of the Secretary, when the note is secured by a mortgage of a vessel. The need for reference to a non-citizen individual arises because an individual cannot qualify as a citizen under section 2 of the Shipping Act, 1916.

12. Section 31328(e). At line 38 on page 10 of the Committee Draft, language should be inserted to make clear that the prohibition on operation of the vessel refers only to a trustee acting as a holder of a preferred mortgage on a documented vessel for the benefit of a person not eligible to be the holder of a preferred mortgage on that vessel. If the trustee is acting for the benefit of a person eligible to be the holder of a preferred mortgage, there is no reason for this restriction on the operation of the vessel by the trustee.

13. Section 31329(d). At line 21 on page 11 of the Committee Draft, the same change should be made as applies to section 31328(e) for the same reasons.

14. Section 12111(c)(2). The provisions of this subsection arguably may be construed to be in conflict with the provisions of section 31327 (page 10 of the Committee Draft, lines 3-7). While section 12111 applies expressly only to certificates of documentation, the legal documentation of a vessel is of course essential to the preservation of the mortgagee's interest, governed by section 31327. We have suggested language to make clear that the provisions of section 12111 are not intended to preempt the applicability of section 31327.

15. Section 12111(c)(3). At line 34 on page 13 of the Committee Draft, the term "preferred" should be deleted and the terms "filed or recorded under chapter 313" should be inserted after the word "mortgage." The purpose of this change is to protect the documented status of the vessel covered by a non-preferred mortgage, as well as a preferred mortgage, against a surrender of the certificate of documentation by the owner.

16. Section 9 of the Shipping Act, 1916, at the third paragraph. The text at line 6 of page 14 should be amended to make clear that the Shipping Act does not require that a documentation citizen, who may not be a citizen under section 2 of the Shipping Act, first obtain approval from the Secretary before bidding at a U.S. Marshal's sale.

17. Section 9 of the Shipping Act, 1916, at the third paragraph. At lines 11 and 12 on page 14 of the Committee Draft, the words "or control" should be deleted. As presently written, the inclusion of this language would change existing provisions of section 9 of the Shipping Act, which speak only of an "interest" in a vessel, and not "any interest or control" in a vessel. We are aware that the Maritime Administration has construed section 9 of the Shipping Act to prohibit the unapproved transfer of "any control" in a U.S. flag vessel, as well as "any interest in the vessel," but we believe this reading of existing law to be erroneous and inconsistent with the decision of United States courts. To include the language prohibiting transfer of "any control" will raise questions of interpretation such as whether the intent is to prohibit an alien from acquiring any shares of a U.S. flag vessel-owning corporation. Such

acquisitions now occur daily on the New York Stock Exchange, for example.

18. Section 1101(a)(2) of the Merchant Marine Act, 1936. At line 27, on page 14, the terms "and recorded" should be deleted. Under sections 31321 and 31322 of chapter 313, a mortgage will become a preferred mortgage "when filed," and not "when filed and recorded."

19. Miscellaneous provision (f). At line 3 on page 15, the term "documented" should be deleted. Under sections 31321 and 31322 of chapter 313, the priorities between maritime liens and preferred mortgages on undocumented vessels will be affected, because mortgages may attain preferred status before the process of documentation is complete.

The Finance Committee has limited its review of the Committee Draft to the foregoing provisions of chapter 313, the provisions of chapter 315 relating to chapter 313, and the definitions in section 30101 of terms appearing in or relating to chapter 313. We have intentionally refrained from commenting upon other definitions of section 30101 and other unrelated provisions of chapter 315 concerning coastwise and fisheries documentation, and the repeal of obsolete laws.

We have excluded from express comment the recently proposed Vessel Identification System legislation including the proposed addition of subsection (d) to section 31322 of H.R. 3105 which would make substantial changes to existing law relating to liens against undocumented vessels titled under state law. We believe this proposal raises many difficult legal questions and technical problems for which there has been insufficient opportunity for review by the Finance Committee and others concerned. We suggest deferral of consideration of this proposal.

In addition to the statutory changes recommended by the Finance Committee, we strongly believe that the legislative history pertaining to this bill will be of great assistance to the maritime and judicial community for purposes of interpretation of this statute in years to come.

We have discussed with members of your Staff that we would be pleased to provide comments on the legislative history before it is finalized.

We thank you for the opportunity to present our views on this legislation, which is of central importance to the maritime community. Please do not hesitate to contact me if the Finance Committee can be of further assistance.

Very truly Yours,

Richard B Barnett

Richard B. Barnett
Chairman
Committee on Marine Finance

Enclosure

cc: Mr. John M. Cullather
Mr. Hugh Johnson
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Richard B. Teiman, Esq.
Chairman, Subcommittee on Recodification